

TOWARD A NEW CAPITALISM



THE ASPEN INSTITUTE
FUTURE OF
WORK
INITIATIVE

A POLICY AGENDA TO RESTORE
THE PROMISE OF WORK



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INITIATIVE

THE FUTURE OF WORK INITIATIVE is a nonpartisan effort to identify concrete ways to strengthen the social contract in the midst of sweeping changes in the workplace and workforce. The Initiative is focused on two key objectives: first, to advance and protect the economic interests of Americans in the independent workforce, including those in the rapidly growing on-demand economy; and second, to inspire a 21st-century capitalism which rewards work, fuels innovation, and promises a brighter future for businesses and workers alike. The Initiative is driven by the leadership of Honorary Co-Chairs Senator Mark Warner and Purdue University President Mitch Daniels with Co-Chairs John Bridgeland and Bruce Reed. For more information visit aspn/futureofwork.

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INTRODUCTION

THE FORCES OF INNOVATION and global competition – combined with an increasing quest for short-run profits at the expense of long-run value – are undermining the partnership between business and workers, and contributing to stagnating wages, economic insecurity, and declining workforce investments.

We need a new model of capitalism that offers novel ways to meet these challenges. Our agenda of new ideas has three overarching goals:

- Workers should benefit from the economic growth their productive capacities help create. That means rising wages and a greater stake in the businesses where they work.
- All workers should have access to critical safety net benefits and protections, no matter their employment classification.
- Workers need more skills, more flexibility, more say, and more opportunities to fulfill their potential and keep pace with the future of work.

Our policy agenda attempts to accomplish these goals by encouraging businesses to reward and invest in their workforce, using three leverage points – business incentives, public information, and corporate governance. Because we recognize not all businesses will respond to these leverage points, we also include policies that empower workers to pursue economic opportunity, security, and training outside of the employment relationship.

Rewarding Businesses for Rewarding Work: Over the past several decades, while competition and innovation have pressured businesses to reduce the cost of labor, policymakers have been focused on creating incentives for investments in physical capital, but not human capital. In fact, although labor and training costs are considered expenses and therefore not taxed, the combination of accelerated depreciation and the tax exemption of debt financing has led to negative effective tax rates on physical capital investment for many industries.¹ As we seek comprehensive tax reform that broadens the base, lowers rates, and simplifies the code, policymakers should also focus on creating a tax and regulatory structure that encourages businesses to reward and invest in the workforce.

Arming Consumers, Workers, and Investors with the Power of Information: Consumers have the power to reinforce their values through the companies they choose to patronize; workers through the places they choose to work; and investors through the businesses

¹ Congressional Budget Office 2014. "Taxing Capital Income: Effective Marginal Tax Rates Under 2014 Law and Selected Policy Options." December. https://www.cbo.gov/sites/default/files/113th-congress-2013-2014/reports/49817-Taxing_Capital_Income_0.pdf

or savings vehicles they choose to fund. That power is surging: technology makes it easier for consumers and workers to make informed decisions; Millennials, who represent a growing share of consumer purchasing power, are more likely to incorporate their values into decisions about what they buy or where they work than previous generations; and investors are increasingly taking social impact into account as they seek financial returns.^{2 3} By providing consumers, workers, and investors with greater information about how well companies pay, train, and schedule their employees, we can empower the market itself to promote a better future of work.

Giving Everyone a Stake in Prosperity: Real, durable growth requires making decisions with a long-term perspective. Policies that give everyone – investors, managers, and workers – a greater stake in a company’s future will make it easier for leaders to take the long view and improve the performance of what should be a mutual enterprise. These proposals encourage worker ownership and involvement in governance, promote long-term shareholding, and dissuade management from succumbing to the pressure to focus only on the short-term.

Empowering Workers to Make the Most of Their Potential: Just as it is important to encourage businesses to reward and invest in the workforce, workers should also have more control over their professional lives. These proposals seek to empower workers by providing them with the tools to improve, the security to persist, the flexibility to make the most of their lives, and the opportunity to get ahead.

² Barton, Fromm, and Egan 2012. “The Millennial Consumer: Debunking Stereotypes.” The Boston Consulting Group. April. <https://www.bcg.com/documents/file103894.pdf>

³ Mudaliar, Schiff, and Bass 2016. “2016 Annual Impact Investor Survey.” The Global Impact Investing Network. May. https://thegiin.org/assets/2016%20GIIN%20Annual%20Impact%20Investor%20Survey_Web.pdf

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REWARDING BUSINESSES FOR REWARDING WORK

1. Lift the Cap on Employer-Provided Education Assistance

POLICY GOAL: To encourage businesses to invest more in the careers of all employees, not just those at the top.

BACKGROUND: For nearly a century, the government has provided incentives for companies to offer health care and retirement benefits. When individuals spent their career with one or two different companies, there was no need to incent businesses to invest in their employees. But as worker tenure has fallen and career employment is increasingly rare, this is no longer the case. This policy option, and the three following it, would recognize that education and training benefits are as important to the future of work as health and pension benefits.

Under section 127 of the Internal Revenue Code, employers may provide and exclude up to \$5,250 in educational assistance for each employee each year. The \$5,250 cap on employer-provided tuition assistance was established in 1986, and is not indexed for inflation. As a result, the value of this exclusion has eroded significantly over the past three decades. If the exclusion had been indexed for general inflation for the past 30 years, the excluded amount would be approximately \$11,393 for 2016. If the exclusion amount had been indexed to higher education tuition inflation, the exclusion would stand at approximately \$26,250 for 2016 (based on tuition increases of 500 percent).⁴

The exclusions for other employee benefits such as retirement benefits and health benefits have increased dramatically over the past three decades. For example, tax-deferred contributions to 401(k) plans have increased from \$7,000 in 1986 to \$18,000 in 2016.^{5 6} The exclusion for employer-provided health care is unlimited, and the average amount excluded has increased over 300 percent in the past three decades.⁷

A recent analysis conducted by the Lumina Foundation and Accenture of Cigna's tuition assistance program found that employer-provided tuition benefits can be highly beneficial to workers, with workers who took advantage of the program seeing their wages grow by 43

4 Jamrisko, Michelle and Kolet 2013. "College Costs Surge 500% in U.S. Since 1985: Chart of the Day." Bloomberg News. 26 August <http://www.bloomberg.com/news/articles/2013-08-26/college-costs-surge-500-in-u-s-since-1985-chart-of-the-day>

5 Investment Company Institute 2006. "401(k) Plans: A 25-Year Retrospective." November. <https://www.ici.org/pdf/per12-02.pdf>

6 Internal Revenue Service 2016. "Retirement Topics - 401(k) and Profit-Sharing Plan Contribution Limits." 28 July. <https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-401k-and-profit-sharing-plan-contribution-limits>

7 Kaiser Family Foundation 2015. "Employer Health Benefits Survey, Exhibit 6.3: Average Annual Worker and Employer Contributions to Premiums and Total Premiums for Single Coverage, 1999-2015." 22 September. <http://kff.org/report-section/ehbs-2015-section-six-worker-and-employer-contributions-for-premiums/>

percent over a three-year period compared to workers who did not participate (entry-level worker wages grew by an even more impressive 57 percent). Turnover also declined by 8 percent, saving the company money on search and training costs.⁸

PROPOSAL: Raise the cap on the income exclusion of employer-provided educational assistance to \$10,000 for non-highly compensated employees, and index it to general inflation.

There is evidence that raising the exclusion cap would increase tuition assistance. According to data compiled by EdAssist, the higher that companies set their own policies for how much tuition they will reimburse, the higher the average annual spend per employee. This effect extends past \$5,250 – for example, companies with no policy limiting how much tuition they will reimburse spent on average over \$10,000 annually per employee on tuition – even when only the first \$5,250 of that could be excluded from taxation. Given that Section 127 represents a significant subsidy for tuition assistance – equal to the taxpayer’s marginal rate, which is generally over 20 percent for middle-income workers – it is likely that this would provide enough incentive for many businesses to raise their tuition caps.⁹ Restricting this policy option to only non-highly compensated employees – defined under ERISA as those currently making under \$120,000 – would help ensure that companies do not use the subsidy to increase their tuition assistance to high-income employees, who already receive a disproportionate share of employer-provided training investments.

The non-discrimination rules currently applicable under section 127 would continue to apply to the expanded benefit. Under current law, employers who offer certain retirement, health care, and education benefits to their employees are subject to rules requiring that non-highly compensated employees receive treatment similar to that of highly compensated employees.

2. Make Employer Payments to Retire Student Debt Tax-Free Compensation

POLICY GOAL: Encourage more employers to promote employee loan debt reduction.

BACKGROUND: Rising student loan debt threatens long-term wealth accumulation for American workers. It also inhibits young workers from investing in their own future by pursuing advanced degrees and certifications. The average 2015 graduate had over \$35,000 in student debt, restricting the ability of workers to seek continuing education opportunities.¹⁰ We should encourage more employers to assist workers in paying down student loans.

Under current law, employers receive a deduction for any interest and debt payments

8 The Lumina Foundation 2016. “Talent Investments Pay Off: Cigna Realizes Return on Investment from Tuition Benefits.” White Paper. <https://www.luminafoundation.org/files/resources/talent-investments-pay-off-cigna-full.pdf>

9 EdAssist 2012. “EdAssist’s Annual Review of Employer Tuition Assistance Programs: Data and Trend Analysis.” 2012 Benchmark Report. <http://www.edassist.com/resources/research-reports-webinars/tuition-assistance-benchmark-report>

10 Sparshott 2015. “Congratulations, Class of 2015. You’re the Most Indebted Ever (For Now).” The Wall Street Journal. 8 May. <http://blogs.wsj.com/economics/2015/05/08/congratulations-class-of-2015-youre-the-most-indebted-ever-for-now/>

made on an employee's behalf. In contrast, employees must take into income as compensation any debt reduction paid for or interest payments made by their employer. This compensation is taxable for both payroll and income tax purposes.

Additionally, if a taxpayer's modified adjusted gross income is less than \$80,000 (\$160,000 if filing a joint return), then the taxpayer may deduct up to \$2,500 in qualified student loan interest expense per year. The cap on the deduction was adjusted upward annually in the late 1990s, but has remained at \$2,500 since 2001.¹¹ According to the Congressional Research Service, taxpayers making under \$50,000 represent over half of the total interest deducted under this provision.¹²

PROPOSAL: This proposal includes two components. First, the cap on the student debt interest deduction would be raised to \$3,400 for 2017 and indexed to inflation thereafter. This is roughly where it would be if it had been adjusted for inflation since 2001.¹³

Second, employer contributions to pay down qualified student debt would be excluded from both income and payroll taxation. This would be accomplished by expanding the existing tax treatment on 401(k) contributions to student debt repayment. The \$18,000 cap on employee 401(k) contributions and the total \$53,000 cap on both employee and employer contributions would apply to the sum of retirement contributions and student debt repayment. The non-discrimination rules that currently apply to 401(k) plans would continue to apply to the expanded benefit as well, and the exclusion would be phased out between \$65,000 and \$80,000 (or \$130,000 to \$160,000 for married filing jointly) which is the same phase-out as the student loan interest deduction.

It is also important that employers are allowed to use these repayments to trigger matching contributions. The most straightforward approach would allow employers to match an employee student loan repayment with their own contribution towards repayment of that loan. Sen. Wyden has proposed a slightly more limited option: Employers would be allowed to treat student loan payments the same as an elective contribution to a 401k plan, thus triggering a matching contribution to the employee's 401(k).¹⁴ Under this latter approach, employers would not be able to make matching contributions towards an employee's student debt, but these employees would still be able to take advantage of employer retirement matching contributions even if their student loan burdens prevented them from making their own retirement contributions. Many young workers have difficulty taking advantage of the favorable tax treatment for retirement contributions because they must also pay down their student loans. Both are forms of long-term savings, and the tax code should treat them in a similar manner.

11 Erb 2011. "Deduct This: The History of Student Loan Interest." *Forbes*. 13 June. <http://www.forbes.com/sites/kellyphil-lipserb/2011/06/13/deduct-this-the-history-of-the-student-loan-interest/#16ea86be3751>

12 Keightley 2011 "An Overview of Tax Benefits for Higher Education Expenses." Congressional Research Service. 11 February.

13 If adjusted for inflation, this deduction would increase to \$3,347. We rounded up to \$3,400.

14 Wyden 2016. "Retirement Improvements and Savings Enhancements (RISE) Act Discussion Draft." Senate Finance Committee. September. <http://www.finance.senate.gov/ranking-members-news/wyden-proposal-would-crack-down-on-tax-avoidance-in-retirement-plans-create-new-opportunities-for-working-americans-to-save>

3. Establish New Tax Incentives to Promote Investment in Worker Training

POLICY GOAL: To encourage businesses to invest more in the careers of their employees through skills training.

BACKGROUND: Despite the growing importance of human capital in creating businesses and remaining globally competitive, policymakers continue to enhance incentives for investment in tangible property while worker investment incentives remain constant. Tax law has moved from accelerated cost recovery to 50 percent write-off of capital costs in the first year, plus accelerated depreciation of the remaining half. Some policymakers are now calling for 100 percent expensing of all capital assets, including buildings. Meanwhile, the tax treatment of worker training expenses has remained constant: deductible by the employer when incurred and not considered additional compensation to the employee.

The fact that the benefits of worker investments are intangible and difficult to quantify makes the playing field uneven. Moreover, the benefits of worker training may not all accrue to the specific company making the investment. The result is an underinvestment in workers that can have significant economic impacts.

Investments in training are also not distributed evenly. Studies show that businesses tend to provide more training to workers that already have high educational attainment and higher earnings.^{15 16} This suggests that policies should aim not only to increase employer-provided training, but also to ensure that the training is fairly distributed.

Worker training tax incentives are common in other countries and at the state level. Most countries in Europe allow for businesses to deduct training costs as expenses for the purposes of determining taxable income, as the U.S. does, but some go further. The Netherlands, for example, allows training expenses to be deducted not just from income for the purposes of the corporate income tax (as most countries allow), but also from the social insurance taxes levied on wages, up to 2,700 euros per year. Austria allows for a 120 percent business deduction for training expenses, as well as a 6 percent credit for companies that don't make enough profit to benefit from the deduction. France provides a business credit for entrepreneurs equal to the number of training hours multiplied by the minimum wage. France and Austria also provide tax incentives for hiring apprentices – given that apprenticeships are training periods by nature, this can be considered another tax incentive for training.¹⁷

The European Union's European Centre for the Development of Vocational Training interviewed 21 experts from across Europe. It concluded that these tax incentives were popular for encouraging training and required less administrative overhead than spending programs, but noted that:

15 Levine, Popovich, and Strong 2013. "Doing Well and Doing Good: Pioneer Employers Discover Profits and Deliver Opportunity for Frontline Workers." The Hitachi Foundation. September. http://www.hitachifoundation.org/storage/documents/DWDG_Web_Final.pdf

16 Lerman, McKernan, and Riegg 2004. "The Scope of Employer-Provided Training in the United States: Who, What, Where, and How Much?" W.E. Upjohn Institute.

17 Cedefop Panorama Series 2009. "Using Tax Incentives to Promote Education and Training." European Centre for the Development of Vocational Training, Office for Official Publications of the European Communities. <http://www.cedefop.europa.eu/en/publications-and-resources/publications/5180>

- Tax incentives may subsidize training activities that would have otherwise been done anyway (this is called “additionality”).¹⁸
- Tax incentives should try to target populations that don’t already have access to training, yet often this targeting requires administrative complexity that discourages take-up.¹⁹

Many states also provide tax incentives for training, including Connecticut, Georgia, Kentucky, Mississippi, Rhode Island, and Virginia. For example, Connecticut provides a business tax credit equal to 5 percent of all expenses incurred for the enhancement of human capital, including training.

There is little evaluation of state tax incentives.²⁰ Nonetheless, an evaluation by Connecticut’s Department of Economic and Community Development found that the credit “produces modest and positive benefits... [including] cumulative productivity gains to firms making investment in human capital.”²¹

PROPOSAL: Establish a tax incentive for worker training. This could take a few different forms:

A. Worker Training Credit. Businesses would be allowed a credit equal to 20 percent of the excess of qualified training expenditures on non-highly compensated workers over the average annual training expenditures incurred in the base period, adjusted for inflation. The base period is defined as the three years immediately preceding the current tax year. So for example, assume an enterprise incurred the following qualified worker training costs for the years 2013-2016:

2013	\$200,000
2014	\$250,000
2015	\$300,000
2016	\$350,000

The average annual training expenditures would be \$250,000 [(200K + 250K + 300K)/(3 years)]. The worker training credit would be calculated for 2016 as follows:

Qualified worker training expenditures 2016	\$350,000
Less: Average annual training expenditures	<u>\$250,000</u>
Excess of qualified worker training expenditures	\$100,000
X applicable percentage	<u>X 20%</u>
2016 Worker Training Credit	\$20,000

¹⁸ Ibid.

¹⁹ Ibid.

²⁰ The Pew Charitable Trusts 2016. “Economic Development Tax Incentives.” <http://www.pewtrusts.org/en/projects/economic-development-tax-incentives>

²¹ Department of Economic and Community Development 2014. “An Analysis of Connecticut’s Tax Credit and Abatement Programs.” State of Connecticut. September. http://www.ct.gov/ecd/lib/ecd/decd_sb_501_sec_27_report_revised_2013_final.pdf

Qualified worker training is training that maintains or improves skills needed in the worker's present job or is part of a program of study that will qualify the worker for a new trade or advancement in their current trade.

Rules similar to those provided under section 41 of the internal revenue code (research and experimentation expenditures) would be applied as needed to minimize rewarding worker investment that would occur in the absence of the credit. While this proposal would be complicated to comply with, business experience with the similar R&E credit should provide guidance.

The tax credits offered in Austria and France, along with Connecticut, Georgia, Kentucky, Mississippi, Rhode Island, and Virginia apply to total training expenses.²² Rep. Pete Aguilar (D-CA) has introduced *On-the-Job Training Tax Credit Act of 2015*, which includes a similar training tax credit.²³ This proposal is similar to those examples, but different in that it subsidizes only the marginal increase rather than the entire training expenditure. Belgium offered a tax credit for training increases – similar to this proposal – from 1999-2001, but it was terminated because it was not consistent with European Commission regulations.²⁴

B. Exclusion of Qualified Worker Training Compensation from Income and Payroll

Taxes. Non-highly compensated employees would be permitted to exclude up to 80 hours (two weeks) of earnings from both wages and income where those hours are spent participating in a qualified worker training program. Employers providing the qualified worker training program would exclude the compensation paid to employees participating in the program for purposes of payroll taxes.

This exclusion would put employer-provided worker training benefits on par with employer-provided retirement and health benefits. Under current law, both retirement and health benefits are excluded from the employee's wages for both income and payroll tax purposes.

There are international precedents for this approach: both the Netherlands and France allow training compensation to be excluded from social insurance taxes.²⁵

C. Pay for Performance.

Businesses that invest in their non-highly compensated workers should share in the upside potential. If a business expends a significant amount on training an employee within a two calendar year period, then for the next three years the business

22 Connecticut: Credit of 5% of all expenses incurred for the enhancement of human capital.
Georgia: Tax credit of 50 percent of a company's direct training expenses, with up to \$500 credit per full-time employee, per training program. Maximum annual credit per employee of \$1,250.
Kentucky: Tax credit of 50% of eligible training.
Mississippi: Tax credit of 50% of costs for training an employee, not to exceed \$2,500 per employee per year.
Rhode Island: Tax credit of 50% of training expenses for all employees, capped at \$5,000 per employee.
Virginia: Tax credit of 30% of training costs (if through community college) or \$200 annually (if through private schooling) for employers who participate in worker retraining efforts.

23 Companies with 500 or fewer full-time employees that also participate in on-the-job employee training would receive the lesser of the following as a tax credit: 50 percent of all expenditures for the job training program or \$5,000. Representative Aguilar introduced the bill on May 19th, 2015 to the House. One key difference is that this bill would subsidize all training expenditures, not just the incremental increase. <https://www.congress.gov/bill/114th-congress/house-bill/2431/actions>

24 Cedefop Panorama Series 2009. "Using Tax Incentives to Promote Education and Training." European Centre for the Development of Vocational Training. Office for Official Publications of the European Communities. <http://www.cedefop.europa.eu/en/publications-and-resources/publications/5180>

25 Ibid. It should be noted that France does this indirectly, by not applying social insurance taxes to apprenticeship wages.

will receive a tax credit equal to a certain percentage (a “recoup rate”) of however much that employee’s wage growth outpaced wage inflation.

For example, assume a worker’s salary during training is \$30,000, and that in the following year she finds a job at \$50,000. If general wage inflation is 2 percent, and the recoup rate were set at 10 percent, then her salary baseline is $\$30,000 * (1 + 2\%) = \$30,600$, and her prior employer would receive a tax credit equal to $10\% * (\$50,000 - \$30,600) = \$1,940$. This tax credit would be capped at the cost of the initial training investment.

4. Deem Repatriation of Offshore Income at a Lower Rate for Earnings Used to Increase Compensation for Low and Middle-Income Employees

POLICY GOAL: To encourage companies to pay higher wages to lower-paid employees, including those previously contracted out.

BACKGROUND: Under current tax law, U.S. companies are taxed on their world-wide income with certain exceptions. One exception is for foreign earnings where the funds have not been repatriated. The U.S. corporate income tax on those earnings is deferred until the monies are brought back to the U.S.

It is difficult to compute how much U.S. companies have earned and kept abroad, because the IRS does not require disclosure of such amounts. However, according to a variety of estimates, at least \$2 trillion of unrepatriated earnings remain abroad.^{26 27} Some of these funds have been invested in companies’ foreign operations, funding expansion of facilities and workforce. Most of it remains available for repatriation or future investment.

For the past several years, mergers of multi-national companies with new headquarters based abroad and the inversion of U.S. companies to move headquarters overseas have highlighted the need to enact international tax reform. Lowering the statutory rate and moving toward a territorial system where foreign earnings are taxed only by the foreign government where profits are earned could reduce the incentive to restructure in order to have a non-U.S. entity as parent of the consolidated corporation.

If Congress does enact a territorial-type system, some transition rule would be necessary to close out the taxation of pre-reform earnings that have not yet been taxed. Firms could be required to repatriate their overseas earnings and pay a one-time tax on these earnings. Most policymakers have concluded that taxing these earnings at 35% is unfair, since that would be much worse than current law, which at minimum allowed for a reduced rate due to the time value of money associated with deferral. Policymakers have suggested tax rates ranging from 3.5% (proposal from Rep. Dave Camp on reinvested foreign earnings) to 14% (Obama 2017 Budget).

In 2004, Congress enacted a temporary repatriation proposal that allowed enterprises to choose to bring home some or all of their deferred earnings at an effective rate of 5.25%. Many

26 Citizens for Tax Justice 2015. “\$2.1 Trillion in Corporate Profits Held Offshore: A Comparison of Different International Tax Proposals.” July. <http://ctj.org/pdf/repatriation0715.pdf>

27 Rubin 2015. “U.S. Companies Are Stashing \$2.1 Trillion Overseas to Avoid Taxes.” Bloomberg. March. <http://www.bloomberg.com/news/articles/2015-03-04/u-s-companies-are-stashing-2-1-trillion-overseas-to-avoid-taxes>

companies chose to do so. A study by the Internal Revenue Service estimates that companies collectively repatriated \$350 billion of foreign earnings.

In retrospect, many policymakers wish they had ensured that the repatriated earnings be used for specific purposes. Most research indicates that a large percentage of the repatriated earnings were allocated to investor payouts and debt reduction.

Providing a lower bifurcated tolling rate – a lower rate on repatriated earnings that are used to raise wages and a higher rate on other repatriated funds – might be a powerful way to boost the wages of lower-income employees.

PROPOSAL: As part of international reform, require that all U.S. companies that own at least 10 percent of a foreign subsidiary would include into income their pro rata share of that subsidiary’s post-1986 earning and profits (E&P). The E&P would be included into income only if it had not been subject to U.S. tax. The E&P amount would be taxed at certain base rate. However, that rate would be reduced by four percentage points on the amount of E&P equivalent to the amount the firm incurred increased qualified compensation expenditures (IQCE). This E&P would be divided by ten, and one-tenth of the amount would be payable in each of the 10 years after enactment.

Increased qualified compensation expenditures (IQCE) are equal to the increase in total compensation – wages and benefits – the firm paid to its non-highly compensated employees in a taxable year compared to the previous taxable year, adjusted for inflation. The tax benefit would be allocated to the subsequent taxable year.

Example:

Assume Multinational had \$10 million in deferred foreign earnings (E&P) that would be subject to the deemed repatriation tax on December 31, 2017, and assume a 12 percent base rate and 8 percent reduced rate.

Multinational would include \$1 million of E&P into earnings in each of the years 2018-2027. For 2018, Multinational will include \$1 million of E&P into income at a base rate of 12 percent, less any amount the company incurred in increased qualified compensation expenditures for 2017 in excess of costs incurred for 2016, adjusted for inflation, which would be subject to the lower 8 percent rate. Assume that Multinational’s 2017 qualified compensation costs were \$6,200,000 and its qualified compensation costs for 2016 totaled \$5,200,000 (inflation adjusted number).

<u>\$6,200,000</u>	<u>2017 Qualified Compensation Expenditures</u>
<u>\$5,200,000</u>	<u>2016 Qualified Compensation Expenditures (inflation adjusted)</u>
<u>\$1,000,000</u>	<u>2018 E&P eligible for the lower rate</u>

In this case, the entire \$1 million in income allocated to 2018 would be eligible for the lower rate.

Assume, however, that the company incurred \$5,800,000 in 2016 Qualified Compensation Expenditures. In that case, \$400,000 of the \$1 million would be taxed at 8 percent and the remaining \$600,000 would be taxed at 12 percent.

In year 2019, Multinational would need to have 2018 Qualified Compensation Expenditures of at least \$7,200,000 plus inflation in order to have its \$1 million allocated to 2019 taxed at the lower 8% rate.

The proposal builds on two principles that have achieved some consensus among policymakers. First, deemed repatriation tax payments should be made over a period of years (usually around a decade). This provides a structure that can encourage multiple real increases in workers' wages. And second, different tax rates can be applied to deemed repatriated earnings based on certain factors. This provides an opening to contrast the value of a lower rate for earnings reinvested in capital assets abroad to earnings reinvested in human capital (workers).

5. Reward Responsible Corporations (R Corps)

POLICY GOAL: To highlight, promote, and reward those businesses that agree to employ a more workforce-oriented growth model, and which adhere to a strict set of verifiable standards.

BACKGROUND: The tax incentives in this section will give businesses a greater stake in their workers, but we believe in offering an additional incentive for businesses willing to go further. For that reason, we propose creating a voluntary new corporate form, called the R Corp, which will be eligible for enhanced incentives in return for broader worker ownership, greater investment in training, and stronger long-term governance.

This approach offers a number of benefits. First, it creates an additional financial incentive for worker-friendly practices beyond the individual incentives, and it includes structural changes like worker ownership that could make those practices harder to abandon in the future. Second, it elevates the brands of individual companies that engage in worker-friendly practices, thus providing another reason for companies to adopt and continue those practices. And finally, there is a growing movement of organizations setting standards and metrics and working with companies to promote more responsible and inclusive business decision-making, but there is little agreement on which standards and metrics to use. The development of the R Corp can and should be complementary to the work of these organizations by helping organize a consensus around specific standards and metrics.

PROPOSAL: To become an R Corp, companies would agree to take on new responsibilities around worker investment, compensation, ownership, and governance. Companies that live up to these responsibilities would be eligible for tax and regulatory relief.

Policymakers should work with organizations with expertise in this space, as well as business and labor leaders, to determine the conditions that businesses must meet in order

to qualify as an R Corp. A starting point could be the following:

WORKER INVESTMENT: Invest as much training in non-highly compensated employees as highly compensated employees. This would be calculated by comparing the average amount spent (per worker) on training non-highly compensated employees to the average amount spent on training highly compensated employees.

PREDICTABLE SCHEDULING: Require that all work sites provide employees with advance notice of work schedules for all workers, and limit on-call scheduling. This would apply to contract employees and independent contractors as well. Unpredictable scheduling makes it difficult for workers with other commitments, such as care-taking duties or higher education, to remain in the workforce.

COMPENSATION: Agree to base executive compensation on long-term returns and increase non-executive compensation at least as rapidly.

EMPLOYEE OWNERSHIP: Commit a significant amount – perhaps at least 25 percent – of the ownership of the company to non-highly compensated workers.

WORKER COUNCILS: Promote worker participation in decision-making by establishing worker councils at each work site. These councils could also help promote company compliance with the other R-Corp commitments. The National Labor Relations Act (NLRA) would also need to be amended to allow such councils.

As an incentive to take on these responsibilities, R Corporations would be eligible for the following tax and regulatory relief:

LOWER CORPORATE TAX RATE: Businesses that file as R Corporations would be subject to a reduced corporate tax rate.

SIMPLIFIED REPORTING: R Corps would be allowed to issue earnings reports on a semi-annual rather than quarterly basis. This parallels the movement in the United Kingdom away from quarterly reporting.²⁸

REDUCED RED TAPE: The IRS would eliminate certain requirements on employee ownership, such as the requirement for employees to exercise Incentive Stock Options within 90 days of leaving the company or being terminated.

²⁸ Dakers 2014. "Quarterly reporting quietly comes to an end." The Telegraph. November. <http://www.telegraph.co.uk/finance/good-news/11231685/Quarterly-reporting-quietly-comes-to-an-end.html>

ARMING CONSUMERS, WORKERS, AND INVESTORS WITH THE POWER OF INFORMATION

6. Require Greater Disclosure of Corporate Pay, Training, and Contracting Practices

POLICY GOAL: Empower consumers and workers with greater information about how well companies – and their contractors – pay and train their workers in order to allow the market itself to promote better workforce practices.

BACKGROUND: In 2015, the SEC adopted a new rule that requires public companies to disclose the ratio of compensation for its CEOs compared to the compensation of its median employee, effective in 2017. The Dodd-Frank Wall Street Reform and Consumer Protection Act mandated the new rule. Other SEC filing requirements ensure that public companies report overall spending on compensation. However, even with the new rule, most companies do not provide a full picture of how they pay, train, or treat their workforce. Companies like Glassdoor are beginning to collect data voluntarily submitted by workers, but it is unclear how accurate and representative they are.

The training data is of particular importance, for two reasons. First, training practices may be uniquely opaque to potential employees (who usually know how much they will be paid prior to accepting a job). And second, while capital markets can determine a business's investments in physical capital and R&D from their Form 10-K (submitted annually to the SEC), there is no standardized method for determining a business's human capital investments. This can potentially lead to capital markets punishing businesses with higher than average human capital investments because they may mistake them for high expense levels.

PROPOSAL: Both public companies and private companies above a certain size should be required to publicly report the distribution of worker compensation, benefits, and training expenditures. Companies should also disclose worker tenure and median compensation by tenure, which would reveal the availability of career paths within the company. Alternatively, the IRS could be required to publish its individual tax return data by firm, with worker data from small firms exempted to keep the data anonymous. Also, companies should be required to disclose enough detail about their contracting relationships to provide the government with a full image of the entire supply chain. The federal government should lead by example by publishing these data on its own operations.

The Center for American Progress recently released a relevant proposal calling for greater training expenditure disclosure.²⁹

7. Develop and Adopt Metrics and a Private Sector Standard of Fair Worker Treatment

POLICY GOAL: Promote the development of a broad, private sector, formal definition of fair worker treatment, and parallel certification process – putting focus on greater disclosure and better data, and enabling the development of new metrics, benchmarks, and research that is tangible for business leaders.

BACKGROUND: Over the years, businesses and consumers alike have recognized the need to agree upon reliable standards of product quality, such as the Good Housekeeping Seal of Approval and UL certification, as well as business standards such as the Better Business Bureau. These efforts – achieved without government intervention – have been good for consumers and businesses alike, increasing trust, quality, and consumer satisfaction.

Consumers, businesses, and workers will gain from a similar effort to develop trusted standards, best practices, and common expectations of what companies should do for workers. In the 20th century, the old social contract helped fill that role. Today, at the very moment that the breakdown of the old social contract has left workers more vulnerable, no agreed-upon standards exist.

There is a rapidly growing movement to promote inclusive business decision-making more broadly: a movement which encourages more businesses to balance and integrate all stakeholders beyond just shareholders. Some organizations have attempted to certify or rank corporations on comprehensive performance metrics that go beyond profits – such as the Standard & Poor’s Environmental & Socially Responsible Index, MIT Professor Zeynep Ton’s Good Jobs Score, or the JUST Capital/Forbes corporate rankings.³⁰ Other groups are working to socialize business decision-making and governance structures that ensure a more inclusive growth model, such as the Coalition for Inclusive Capitalism and Conscious Capitalism. Standardized metrics have been developed by organizations like the Sustainability Accounting Standards Board (SASB) and B Lab (which claims an impressive 50,000 businesses using its tool) to better compare corporations across a broad range of alternative criteria.

When it comes to promoting more inclusive workforce practices, this movement faces a number of challenges that federal policy could help address. First, there is a lack of good public data on pay, training, and other workforce practices. The aforementioned organizations have worked hard to collect data where it is available, but this can be imprecise and labor intensive, and much of the data available come from voluntary disclosures. Greater and more detailed public disclosure would be helpful to providing a fuller and more repre-

29 Hanks, Gurwitz, Duke, and Green 2016. “Workers or Waste? How Companies Disclose—or Do Not Disclose—Human Capital Investments and What to Do About It.” Center for American Progress. June. <https://www.americanprogress.org/issues/economy/report/2016/06/08/138706/workers-or-waste/>

30 Ton 2016. “The Good Jobs Score 2016.” <http://www.goodjobsscore.com/>; JUST Capital 2016. “JUST Capital and Forbes Release Inaugural “JUST 100,” Ranking Companies Performing Best on American Public’s Priorities.” November 30. <https://justcapital.com/just-press/2016/11/30/final-press-release>

sentative picture of labor practices across the economy – and by working with organizations already leading in the inclusive capitalism community, we can identify what data points will be most helpful. Second, while much of this movement has had success in coalescing around specific standards and metrics for environmental sustainability, community engagement, social impact, and other positive business practices, there hasn't been community-wide consensus on which standards and metrics should be used to measure workforce practices – a situation in which different organizations develop and publish their own standards and metrics could be confusing to the general public.

PROPOSAL: The President and Congress should create an independent commission of consumers, workers, and business leaders charged with developing an agreed-upon set of non-governmental metrics and standards which can help tangibly and consistently define fair worker treatment – taking into account ideas and input from stakeholders across the spectrum, including civic, business, and labor leaders, academics and policy minds, foundation heads and thinkers from the numerous organizations already leading in this space. Such criteria would help investors, workers, customers, and the public at large know how companies measure up on pay, training, employee ownership, benefits, and scheduling – thus enabling better decision-making by all stakeholders.

8. Create a National Award for Rewarding Work

POLICY GOAL: To publicly highlight companies that are doing right by their workers, honor best practices, and provide an incentive for companies to compete to do better.

BACKGROUND: Many challenges workers face in the 21st century result from a race to the bottom. Companies today have every incentive to cut costs to show near-term profits, at the expense of longer-term value creation – and too often these pressures leave workers behind. These pressures move companies to outsource more jobs, reduce human capital investment, and keep wages stagnant. When one company cuts costs in favor of near-term profits, others are at a competitive disadvantage in the eyes of investors if they don't follow suit. We should do what we can to reverse those incentives by encouraging the opposite – a race to the top that rewards companies for adopting better workforce policies than their competitors.

PROPOSAL: Create a new national award, similar to the Malcolm Baldrige National Quality Award, to highlight companies for excellence in worker advancement. The Baldrige Award – which is given by the President annually to as many as 18 organizations across six eligibility categories – has been highly successful at promoting management best practices and encouraging businesses and their leaders to reform their thinking and decision-making. Further, the Baldrige Award's impact was nearly immediate upon its creation – one Harvard Business Review article praised that “In just four years, [it] has become *the* most important catalyst for transforming American business,” as businesses raced to conduct internal

assessments and improvements to out-do their competitors.³¹ A new award to highlight companies that exhibit the most worker-friendly policies across compensation, ownership, training, and scheduling could have the same impact.

9. Collect Better Data on Employer-Provided Training

POLICY GOAL: To inform businesses and policymakers regarding the state of employer-provided training.

BACKGROUND: While the available data suggests that employer-provided training is falling, the data on such training is sparse. It is inherently difficult to compile because, if the training is conducted in-house, it is hard to disentangle from overall labor costs. The last major federal survey – the BLS Survey of Employer-Provided Training – was conducted in 1995. It is important for both businesses and policymakers to understand the nature of this decline in employer-provided training, and how it may affect the ability of U.S. businesses to find qualified workers and compete globally.

PROPOSAL: Collect data from stratified, nationally representative sample of employers on their training practices (including informal training), spending on training, the integration of work-based training with outside training providers, and their expectations of other providers of occupational training. The survey should also target a selection of firms that offer intensive programs that develop occupational mastery, including unregistered apprenticeship programs. This was proposed by Robert Lerman in a paper for the National Academy of Sciences, and a similar option was proposed by the Center for American Progress.^{32 33} President Obama has also proposed \$3 million in his FY2017 budget for the first year of activities for a survey of employer-provided training, though it is unclear if it will be funded.³⁴

31 Garvin 1991. "How the Baldrige Award Really Works." Harvard Business Review. November-December. <https://hbr.org/1991/11/how-the-baldrige-award-really-works>

32 Lerman 2015. "Are Employers Providing Enough Training? Theory, Evidence and Policy Implications." Prepared for the National Academy of Sciences Symposium on the Supply chain for Middle-Skill Jobs: Education, Training, and Certification Pathways, June. http://sites.nationalacademies.org/cs/groups/pgasite/documents/webpage/pga_168146.pdf

33 Hanks, Gurwitz, Duke, and Green 2016. "Workers or Waste? How Companies Disclose—or Do Not Disclose—Human Capital Investments and What to Do About It." Center for American Progress. June. <https://www.americanprogress.org/issues/economy/report/2016/06/08/138706/workers-or-waste/>

34 Bureau of Labor Statistics 2016. "FY 2017 Congressional Budget Justification." <https://www.dol.gov/sites/default/files/documents/general/budget/CBJ-2017-V3-01.pdf>
Warner 2016. "Press Release: Fifteen Senators Call for Labor Dept. to Survey Contingent Workforce & Employee Training." Office of Senator Mark Warner. 22 March. http://www.warner.senate.gov/public/index.cfm/mobile/pressreleases?ContentRecord_id=53514CE4-DF4A-44BE-95F0-FC55082B3A34

GIVING EVERYONE A STAKE IN PROSPERITY

10. Expand Executive Stock and Profit-Sharing Compensation Systems to All Workers

POLICY GOAL: To encourage more broadly-shared worker ownership and profit-sharing.

BACKGROUND: Worker compensation has stagnated in part because business profits are increasingly diverted to business owners. One solution to this problem is to encourage workers to own more of the companies they work for, thus aligning the interests of workers, managers and investors, and ensuring that their compensation will grow along with the performance of the firm. A similar solution is to tie worker compensation directly to company profits.

Greater worker ownership and profit-sharing entails a number of benefits to businesses and the economy. It is associated with greater employment stability, higher firm productivity, profitability, and longevity. If coupled with greater worker participation in decision-making, it also leads to higher job satisfaction, organizational commitment, identification, motivation, and workplace participation.^{35 36} By strengthening employees' stake in the firm, ownership increases worker motivation and commitment.³⁷

Worker ownership in particular has two additional benefits. First, worker-investors can reduce the short-termism pressures on management, as their investor preferences will likely be more aligned to long-term value creation (in particular worker training) than other investors. And second, ownership enables workers to benefit from innovation and productivity growth, not simply be threatened by it. If companies continue to substitute machines and computers for human activity, worker-owners would benefit from having a stake in the upside of this trend.³⁸

Despite the benefits to both workers and firms, worker ownership and profit-sharing is rare. Fewer than half of workers participate in programs in which worker pay or the wealth of workers (through equity ownership) is directly tied to workplace or firm performance.³⁹

35 Freeman 2007. "Effects of ESOP Adoption and Employee Ownership: Thirty Years of Research and Experience." University of Pennsylvania ScholarlyCommons. Working Paper. January. http://repository.upenn.edu/cgi/viewcontent.cgi?article=10018-context=od_working_papers

36 Brill 2012. "An Analysis of the Benefits S ESOPs Provide the U.S. Economy and Workforce." Matrix Global Advisors. July. <http://community-wealth.org/sites/clone.community-wealth.org/files/downloads/paper-brill.pdf>

37 Akerlof and Kranton 2005. "Identity and the Economics of Organizations." Journal of Economic Perspectives. Winter. <http://public.econ.duke.edu/~rek8/identityandtheeconomicsoforganizations.pdf>

38 Freeman 2015. "Who owns the robots rules the world." IZA World of Labor. May. <http://wol.iza.org/articles/who-owns-the-robots-rules-the-world-1.pdf>

39 Freeman, Blasi, and Kruse 2010. "Shared Capitalism at Work: Employee Ownership, Profit and Gain Sharing, and Broad-based Stock Options." National Bureau of Economic Research. April. <http://www.nber.org/chapters/c8085.pdf>

Ownership and profit-sharing is, however, quite common among the incentive pay packages of business executives. This proposal offers companies a choice: if they want their executive compensation plans to be tax deductible, they must offer similar opportunities to their non-executive workers.

PROPOSAL: To retain the tax deductibility of incentive compensation systems that provide ownership opportunities or link pay to firm performance, firms must (1) extend these compensation systems to all of the company's full-time employees; and (2) ensure that the value expended on the bottom 80 percent of employees by salary is at least as large as the value expended on the top 5 percent of employees by salary. This was first proposed by Richard B. Freeman, Joseph R. Blasi, and Douglas L. Kruse in a paper for the Center for American Progress.⁴⁰

11. Make Stock Compensation Tax-Free

POLICY GOAL: To encourage corporations to facilitate employee ownership of company stock as part of a comprehensive compensation plan.

BACKGROUND: Giving employees an ownership stake in the company can incentivize workers to contribute in ways that will increase the overall value of the company. An ownership stake will also encourage workers to seek advancement within the company as a means of further contributing to the value of the enterprise.

Under current law, health and some transit benefits are excluded from the payroll and income tax, and retirement benefits are tax-deferred. Stock compensation, on the other hand, is currently subject to both income and payroll taxes.

PROPOSAL: Qualified stock compensation should be excludible from income tax and payroll tax for non-highly compensated workers. The company could claim a deduction for the value of the stock on the date of the award. The company would not pay payroll taxes on the stock compensation. The worker would pay neither payroll nor income tax on the value of the stock; however, his or her basis in the stock would be \$0. Qualified stock compensation would be required to meet the following:

1. The stock must be of the company for which the recipient is an employee (or an independent contractor).
2. Companies with over 100 employees must offer a defined contribution plan for the recipient employee and must match employee contributions at the safe harbor level – a full match on the first three percent of compensation, 50 percent match on the next two percent of compensation – in order to be able to grant qualified stock compensation.

⁴⁰ Freeman, Blasi, and Kruse 2011. "Inclusive Capitalism for the American Workforce: Reaping the Rewards of Economic Growth through Broad-based Employee Ownership and Profit Sharing." Center for American Progress, March. https://cdn.americanprogress.org/wp-content/uploads/issues/2011/03/pdf/worker_productivity.pdf

3. The amount of qualified stock compensation is limited to the lesser of (a) 10 percent of the employee's total compensation for the year; (b) 10 percent of the threshold established by the IRS for highly compensated employees, which is currently set at \$120,000.
4. Companies would be permitted to make qualified stock compensation elective (employee chooses taxable cash or tax-free stock) or mandatory on the part of the employee.
5. Companies would be able to make a determination by a date certain as to whether qualified stock compensation would be issued for a particular year.

12. Defer Taxes on Stock Options

POLICY GOAL: To encourage more broadly-shared worker ownership and profit-sharing.

BACKGROUND: The tax code makes it more difficult for private companies to share ownership among their workers by devaluing stock options as a form of compensation for low-income workers. There are two types of stock options: Non-qualified Stock Options (NSOs) and Incentive Stock Options (ISOs). NSOs are taxed when they are exercised – the differential between the value of the stock when the option is granted and when it is exercised is taxed at ordinary income rates. The problem is that many employees have to exercise their options when they leave the company, but can't afford to pay the tax – nor can they easily sell shares to help cover the costs when the company is not publicly traded. In effect, this means that workers with less wealth or limited liquidity are often unable to take advantage of the options during the allotted window after departing a company – being forced to forfeit their options, borrow to cover the tax costs, or sell their options on a secondary market. This isn't a problem for public companies whose shares can be sold anytime, but private companies don't have a liquid market for equity.

ISOs have a different problem. While they are not subject to ordinary income taxation when they are exercised, they are subject to the AMT. This can also lead to a high tax liability when an employee departs the company.

PROPOSAL: For NSOs, defer the ordinary income tax liability until the time of sale rather than the time of exercise. This means that at the time of sale, the holder would have to pay both ordinary income tax (on the difference between the value when granted and the value when exercised) and capital gains (on the difference between the value at the point of exercise and the value at sale). For ISOs, give the holders the option to exercise as if their option were an NSO, which would subject them to the ordinary income tax at the time of sale rather than the Alternative Minimum Tax (AMT) at the time of exercise.

13. Establish Worker Representation on Councils and Boards

POLICY GOAL: To encourage worker participation in company management decisions

BACKGROUND: Greater worker participation in decision-making can lead to higher job satisfaction, organizational commitment, identification, motivation, and workplace participation.⁴¹⁻⁴² One of the reasons is that ownership can tie employees' identities to the firm, which is key to motivating workers and enhancing employee commitment.⁴³ Another reason is that workers are more motivated when they feel they have control over how they do work: an experiment with assembly line workers found that when they were able to control the speed of the assembly line, they actually chose to work *faster*.⁴⁴

A recent Corporate Executive Board survey of over 6,500 employees and 100 heads of HR around the globe found that when making internal changes in the firm (such as restructuring, merging, expanding, etc.), including employees in the decision-making and implementation significantly increases the chance of success and shortens the implementation period by as much as one-third.⁴⁵

Worker representation in the U.S. is almost exclusively provided through labor unions. In most European countries, other vehicles for worker participation supplement labor unions. Germany uses "co-determination," in which workers are represented by work councils and elect their own representatives to the board. If a company employs more than 2,000 workers, half its supervisory board members must be elected by the workers (in Germany, the management board makes company decisions and the supervisory board oversees it).

PROPOSAL: Congress should explore allowing work councils (which are now forbidden by the NLRA) and requiring companies above a certain size to allow its employees to elect a certain share of its board members. This was proposed by Mike Konczal, J.W. Mason, and Amanda Page-Hoongrajok in a paper for the Roosevelt Institute.⁴⁶

14. Expand Long-Term Shareholder Voting Rights

POLICY GOAL: To empower long-term investors to direct the company's resources towards more long-term value creation.

BACKGROUND: There is evidence that long-term shareholders are more likely to monitor the decisions of management and act to ensure that long-term considerations are taken into account. One solution to the challenges posed by short-termist pressures would be to grant long-term shareholders greater power within companies. Many privately held enterprises provide differential voting rights to long-term shareholders. However, U.S. exchange list-

41 Freeman 2007. "Effects of ESOP Adoption and Employee Ownership: Thirty Years of Research and Experience." University of Pennsylvania, ScholarlyCommons. Working Paper. January. http://repository.upenn.edu/cgi/viewcontent.cgi?article=10019&context=od_working_papers

42 Brill 2012. "An Analysis of the Benefits S ESOPs Provide the U.S. Economy and Workforce." Matrix Global Advisors. 25 July. <http://community-wealth.org/sites/clone.community-wealth.org/files/downloads/paper-brill.pdf>

43 Akerlof and Kranton 2005. "Identity and the Economics of Organizations." Journal of Economic Perspectives. Winter. <http://public.econ.duke.edu/~rek8/identityandtheeconomicsoforganizations.pdf>

44 Ulrich 1998. "Intellectual Capital = Competence x Commitment." MIT Sloan Management Review. 15 January 1998. <http://sloanreview.mit.edu/article/intellectual-capital-competence-x-commitment/>

45 Corporate Executive Board Leadership Council 2016. "Open Source Change: Making Change Management Work." Chicago, 26 April.

46 Konczal, Mason, and Page-Hoongrajok 2015. "Ending Short-Termism: An Investment Agenda for Growth." The Roosevelt Institute. November. <http://rooseveltinstitute.org/wp-content/uploads/2015/11/Ending-Short-Termism.pdf>

ing standards prohibit extra-vote shares for public companies unless they had a dual-share structure prior to their IPO (which tends to limit extra-vote shares to founders, family, and long-time managers). This also creates a disincentive for going public, causing many companies to be cut off from the large and liquid public capital market.

Other countries are moving beyond simply allowing businesses to issue extra-vote shares and are actually requiring it. In 2014, France passed the Florange Act, which, among other provisions, automatically doubles the voting power for investors that have held shares for over two years. Only with a two-thirds majority vote can a company opt-out of this voting arrangement.

Oftentimes, the power to nominate is as important as the power to vote. Corporate boards usually nominate executives. If a shareholder wants to nominate someone else, they need to spend their own money to send out a separate ballot, which is costly. “Proxy access” allows a shareholder to place their candidate on the company’s ballot; currently, companies can voluntarily adopt proxy access, but there is no requirement to do so. Dodd-Frank affirmed that the SEC had the authority to require proxy access, and in response the SEC passed Rule 14a-11 which stated that if a shareholder held at least 3 percent of a company’s shares for at least three years, that shareholder could nominate either 25 percent of a board or one member, whichever is greater. This rule was struck down by the D.C. Circuit Court because it found that the SEC did not fully consider the economic impact of the rule.

PROPOSAL: First, provide long-term shareholders with extra votes per share. This could be done either by having stock exchanges change their listing requirements to allow the issuance of extra-vote shares, or by passing a law – similar to the Florange Act – that requires companies to provide long-term investors with extra votes. Second, the SEC should appeal the ruling that struck down its proposed proxy access requirement, and it should strengthen its rule by reducing both the ownership requirement and substantially lengthening the holding time to better target long-term investors. This was proposed by Mike Konczal, J.W. Mason, and Amanda Page-Hoongrajok in a paper for the Roosevelt Institute.⁴⁷

15. Align Institutional Investor Voting with the Interests of their Long-Term Investors

POLICY GOAL: To ensure that long-term investors are adequately represented in corporate governance.

BACKGROUND: As noted earlier in this report, pressure from activist investors have pushed businesses to focus on short-term profits over long-run value creation. But most individual investors are actually saving for the long-term, for college and retirement. These investors are not well-represented in corporate governance decisions.

⁴⁷ Ibid.

Mutual funds can provide a healthy bulwark against this relentless short-term focus. However, index funds – one of the most common types of mutual funds – are not very active in exercising their voice and judgement. This is because the voting decisions for index funds generally flow down to all funds on an issuer by issuer basis, leading index funds to sometimes vote yes and no on the same corporate decision. This results in activist investors having a disproportionate voice in corporate governance.

Furthermore, private equity funds are much more patient investors, and may be a better vehicle for long-term oriented individual investors. But regulatory barriers lock 401(k) investors out of the private equity market.

PROPOSAL: Institutional investors, including mutual and pension funds, must have voting policies that are specifically tailored to the investment horizons of their investors. Specifically:

- Index funds should vote in a manner that reflects the long-term investment horizon of their investors.
- Index funds should not rely on proxy advisory firms that do not provide index-fund-specific voting guidance.
- Mutual funds that accept 401(k) and college savings investments must have voting policies in place that take into account the long-term horizons of their investors.

401(k) investors should also be provided with vehicles issued by private equity in which they can invest.

These ideas are drawn from Delaware Judge Leo E. Strine, Jr.⁴⁸ More work needs to be done to determine how these ideas would be operationalized into policy changes.

16. Limit Stock Buybacks

POLICY GOAL: To promote business investment by limiting the use of stock buybacks.

BACKGROUND: Stock buybacks refer to the act of a business buying back its own stock, either on the open market or as a direct transaction with a current stockholder. A buyback is essentially the opposite of issuing stock: instead of a business raising capital at the cost of diluting its existing shares, it is paying money to buy shares and increase the price of its existing shares. This can leave companies with less money to invest in value-creation.

In the wake of the Great Depression, insider trading rules were put into place that had the effect of limiting stock buybacks, which could be seen as a form of insider trading. But in 1982, the SEC adopted regulation 10b-18, a “safe harbor” rule that guarantees companies will not be charged with insider trading for engaging in buybacks as long as the volume of the buyback is less than 25 percent of the average daily trading volume over the previous four weeks. This gave companies a freer hand to engage in buybacks.

The response to this policy change was immediate. In 1981, stock buybacks consumed

⁴⁸ Strine 2015. “Securing Our Nation’s Economic Future: A Sensible, Nonpartisan Agenda To Increase Long-Term Investment and Job Creation In The United States.” Keynote Address to First Annual American College of Governance Counsel Dinner. 30 October. <http://corpgov.law.harvard.edu/wp-content/uploads/2015/11/Securing-Our-Nation-Intermediate-Final.pdf>

2 percent of net income for the 248 companies continuously listed in the Fortune 500. In each subsequent decade after the rule change, buybacks rose significantly: 25 percent of net income between 1984 and 1993, 37 percent between 1994 and 2003, and 47 percent between 2004 and 2013. Between buybacks and dividends, total payouts now consume roughly 85 percent of net income.⁴⁹

As William Lazonick of the Brookings Institution points out, stock buybacks aren't inherently bad for the economy: this can be an effective way for executives with significant ownership stake to consolidate their ownership, thereby insulating themselves against activist investors and promoting a long-term perspective.⁵⁰

But the empirical evidence suggests that that is not how businesses are using buybacks anymore. Prior to the rule change, if a company became more profitable, it would increase its investments. But that relationship has deteriorated, and now higher profits simply lead to more buybacks.⁵¹ This appears to happen for two reasons. First, corporate executives are using buybacks to enrich themselves – stock-based instruments make up the majority of their pay, so as the stock price rises in response to the buyback, so too does their stock-based compensation. Second, this rising stock value can make it easier to hit quarterly earnings targets, which are often measured relative to the supply of shares.⁵²

These buybacks leave companies with less capital for long-run investments. Empirical data confirms that firms that engage in buybacks subsequently reduce their investment levels.⁵³

Stock buybacks are an activity that, as practiced today, offer little economic value and instead serve to crowd out long-run investments and enrich executives. Total payouts to shareholders now exceed corporate profits.⁵⁴ Value-creation has been replaced with value-extraction.

PROPOSAL: The SEC should require greater disclosure of daily buyback activity and consider rules to prevent executives from benefiting from buybacks. It should also consider either repealing rule 10b-18 or requiring that companies wishing to buy back their shares must increase the wages of their workers by an equal amount.

First, companies should report their daily buyback activity to the SEC. Surprisingly, the SEC does not collect this data, preventing it from even studying violations of the existing rule and how buybacks affect investments: in response to a request from Sen. Tammy Baldwin (D-WI), SEC Chair Mary Jo White explained that “[p]erforming data analyses for issuer stock repurchases presents significant challenges because detailed trading data regarding

49 Lazonick 2015. “Stock buybacks: From retain-and-reinvest to downsize-and-distribute.” The Brookings Institute, Center for Effective Public Management. April. <http://www.brookings.edu/~media/research/files/papers/2015/04/17-stock-buy-backs-lazonick/lazonick.pdf>

50 Lazonick 2014. “Profits Without Prosperity: Stock buybacks manipulate the market and leave most Americans worse off.” Harvard Business Review. September. https://hbr.org/resources/pdfs/comm/fmglobal/profits_without_prosperity.pdf

51 Mason 2015. “Disgorge the Cash: The Disconnect Between Corporate Borrowing and Investment.” The Roosevelt Institute. February. <http://rooseveltinstitute.org/disgorge-cash-disconnect-between-corporate-borrowing-and-investment-1/>

52 Lazonick 2014.

53 Almeida, Fos, and Kronlund 2015. “The Real Effects of Share Repurchases.” Journal of Financial Economics. June. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2276156

54 Mason 2015a. “Understanding Short-Termism: Questions and Consequences.” The Roosevelt Institute. November. <http://rooseveltinstitute.org/wp-content/uploads/2015/11/Understanding-Short-Termism.pdf>

repurchases is not currently available.”⁵⁵

The SEC should also explore rules to prevent executives from benefiting from buybacks. Executive incentive pay is a main driver of stock buybacks – for example, there is evidence that executives time buybacks to when they exercise their own personal options so that the act of exercising does not dilute the value of the stock.⁵⁶ By severing the link between stock buyouts and executives’ own personal gain, buyouts will likely become less frequent and, when they do occur, more aligned to the long-run interest of the business.

Finally, the SEC should consider either repealing safe harbor, i.e. rule 10b-18, or requiring that companies wishing to buy back their shares must increase the wages of their workers by an equal amount (above an inflation-adjusted baseline). Note that repeal of rule 10b-18 would not completely eliminate the ability of companies to repurchase their stock. Tender offers – in which companies buy directly from a shareholder rather than on the open market – do not fall under the rule. And companies could still buy their own shares on the open market, just with the understanding that a large purchase may create legal liability. In other words, this action would make it more difficult to initiate large-scale buybacks while at the same time preserving some flexibility on the part of firms to manage the supply of their stock.

Variations of these policies were proposed by Mike Konczal, J.W. Mason, and Amanda Page-Hoongrajok in a paper for the Roosevelt Institute; by William A. Galston and Elaine C. Kamarck in a paper for the Brookings Institution; and by William Lazonick in a paper for the Harvard Business Review.^{57 58 59}

17. Graduated Capital Gains Rate Based on Holding Period

POLICY GOAL: To encourage investors to hold onto shares longer and promote a more long-term perspective.

BACKGROUND: The current capital gains tax offers a differential rate based on how long the asset is held. If the asset is held for less than one year, then ordinary income tax rates – top rate of 39.6 percent – are applied on the gains. If the asset is held for more than one year, then preferential rates – top rate of 20 percent – are applied on the gains.

There is evidence that long-term shareholders are more likely to monitor the decisions of management and act to ensure that long-term considerations are taken into account. The structure of the capital gains tax rate can be used to encourage more investors to hold onto shares for longer periods of time, which could promote a more long-term perspective by lessening the pressures on management to focus on short-term profits.

PROPOSAL: For taxpayers in the top bracket, assets held for less than one year would be

55 Lazonick 2016. “How Stock Buybacks Make Americans Vulnerable to Globalization.” The Academy Industry Research Network. AIR Working Paper. March. http://www.theairnet.org/v3/backbone/uploads/2016/03/Lazonick.BuybacksAndGlobalization_AIR-WP16-0301.pdf

56 Bens, Nagar, Skinner, and Franco Wong 2003. “Employee Stock Options, EPS Dilution, and Stock Repurchases.” *Journal of Accounting and Economics*. December. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=472968

57 Konczal, Mason, and Page-Hoongrajok 2015.

58 Galston and Kamarck 2015. “More builders and fewer traders: a growth strategy for the American economy.” The Brookings Institute, Center for Effective Public Management. June. <http://www.brookings.edu/~media/research/files/papers/2015/06/30-american-economy-growth-strategy-galston-kamarck/cepmlastonkamarck4.pdf>

59 Lazonick 2014.

taxed at ordinary rates, or 39.6 percent, as under current law. Assets held for longer than one year would be taxed according to a declining rate scale. Assets would need to be held for ten years to be subject of the current 20 percent top rate. Moreover, assets held for more than ten years would be subject to a further declining rate, down to 10 percent for 15 years.

This sliding scale tax rate would constitute a tax increase for individuals selling assets held between one and 10 years and a tax cut for individuals selling assets held longer than 10 years, leading investors to hold stocks for longer periods of time. According to estimates provided by the Tax Foundation, under this proposal the share of stocks held for six years or longer would rise from 35 percent to 52 percent.⁶⁰

Comparable sliding scale increases and reductions would be made on long-term capital gains taxed at rates other than 20 percent (e.g., section 1259 recapture, small business stock, empowerment zone stock).

18. Equalize the Accounting Treatment of Human Capital and Physical Capital Investments

POLICY GOAL: To encourage more human capital investment by reversing the current accounting bias against it.

BACKGROUND: Accounting conventions can have a significant impact on business decisions, especially in an age of activist investors that are more sensitive to quarterly financial metrics. The costs of investments in physical capital are spread over the life of the asset in order to match the cost with the benefit over time, and to ensure accounting neutrality between one-year expenses and long-term investments. But the costs of human capital investments show up entirely in the year in which they are incurred.⁶¹

This disparity in accounting treatment creates a bias in favor of physical investments and consumption (decisions whose benefits accrue immediately) and against human capital investments. Research shows that accounting treatments do indeed change behavior: a study looking at the United Kingdom's voluntary shift from expensing to capitalizing R&D costs found that expensing causes firms to reduce investment outlays.⁶²

PROPOSAL: Call on FASB to explore how financial accounting standards can be revised to treat investments in human capital similarly to investments in physical capital. This is similar to a proposal offered by Robert Lerman in a paper for the National Academy of Sciences.⁶³

⁶⁰ Estimate provided by the Tax Foundation.

⁶¹ PricewaterhouseCoopers 2010. "Accounting for innovation: The impact on technology companies of accounting for R&D activity under IFRS." IFRS industry series. March. <https://www.pwc.com/us/en/issues/ifrs-reporting/assets/ifrs-technology-accounting-r-d.pdf>

⁶² Oswald, Simpson, and Zarowin 2016. "Capitalization vs Expensing and the Behavior of R&D Expenditures." February. Available at SSRN. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2733858

⁶³ Lerman 2015. "Are Employers Providing Enough Training? Theory, Evidence and Policy Implications." Prepared for the National Academy of Sciences Symposium on the Supply chain for Middle-Skill Jobs: Education, Training, and Certification Pathways. June. http://sites.nationalacademies.org/cs/groups/pgasite/documents/webpage/pga_168146.pdf

EMPOWERING WORKERS TO MAKE THE MOST OF THEIR POTENTIAL

19. Experiment with Portable Benefits Models

POLICY GOAL: To provide workers with greater economic security by giving them access to flexible and portable benefits outside of a full-time, formal employment relationship.

BACKGROUND: Much of today's social safety net is provided through formal employment. Workers must be employed – and not independent contractors – in order to access unemployment insurance, workers compensation, short-term disability insurance, and paid time off for illness, vacation, and maternity/paternity (though some states have begun to expand some benefits to independent contractors under certain programs⁶⁴). Social Security and the Affordable Care Act do provide portable retirement, long-term disability, and health care benefits, but they are only partial solutions: Social Security only replaces about 40 percent of the average earner's pre-retirement income (meaning that workers must supplement this income with personal retirement savings, which are largely administered through employer plans) and most workers still receive health coverage through their job.⁶⁵

But the nature of work relationships is changing. More and more workers are in alternative work arrangements, making it more difficult for those workers to access many of the benefits – and tax advantages of pre-tax contributions – traditionally associated with full-time employment. Even employment itself isn't a guarantee of benefits. Many part-time or temporary W-2 employees are left out of many of the benefits and protections afforded to full-time workers, such as paid time off or mandated employer-provided coverage under the Affordable Care Act. And even among full-time employees, coverage isn't as generous as it used to be. More than 80 percent of workers lack a defined benefit retirement plan, and many that have 401(k)s don't receive retirement contributions from their employers.⁶⁶ Access to affordable benefits options that aren't tied to employers is important for all workers.

PROPOSAL: Challenge cities, states, and companies to pilot new benefit models. Support state-level pilots through a Benefits Innovation Fund.

With the fast growth of on-demand economy companies such as Uber and Instacart, the

⁶⁴ Some states do have policies that extend some of these benefits and protections to independent contractors working within the state – but this is by no means the norm. Recent changes in law in New York and Rhode Island, for instance, extended certain FMLA policies to include independent contractors, while California and other states allow independent contractors to opt-in to state level disability insurance.

⁶⁵ Biggs and Springstead 2008. "Alternate Measures of Replacement Rates for Social Security Benefits and Retirement Income." Social Security Administration, Office of Retirement and Disability Policy. Social Security Bulletin, Vol. 68, No. 2. <https://www.ssa.gov/policy/docs/ssb/v68n2/v68n2pl.html>

⁶⁶ Wiatrowski 2012. "The last private industry pension plans: a visual essay." Bureau of Labor Statistics. <http://www.bls.gov/opub/mlr/2012/12/art1full.pdf>

question of benefits for independent workers has noisily arrived in nearly every jurisdiction in the country. Mayors and Governors have expressed interest in developing new models to support these and other workers in alternative arrangements – and to enable the innovative industries providing new and exciting services and work opportunities – but such a program would require significant policy and political work, and potentially public funding to support new efforts, such as through grants for pilot projects. But despite being difficult, this work is important for workers, businesses, and policymakers alike. Without a proper evidence base of what new models might work, it is difficult for leaders in Washington and around the country to even begin to rethink the social contract for a new generation – much less know how to get it right. Meanwhile, if independent workers do not have access to benefits and protections through their job, nor through a system of portable benefits, they will be forced to rely more heavily on the public safety net – at a significant cost to taxpayers.

We believe a fund to support potential pilots would help to catalyze these efforts, and bring to the table the right group of stakeholders in each community – elected officials, labor, worker advocates, and companies. Fortunately, the President’s FY2017 budget proposed a vehicle that could be used to support such pilots – a \$100 million grant fund from the Department of Labor and a \$5 million grant fund from the Federal Conciliation and Mediation Services to support innovative new models. These funds would likely create significant momentum toward pilots on the ground, and serve as catalysts for local action.

What would such a system of portable benefits look to achieve? In November of 2015, a bipartisan and cross-sector coalition of over 40 on-demand platforms, worker advocates, and leading thinkers in policy and civil society came together to agree to a set of principles to which portable benefits for independent workers should adhere. This coalition suggested that any new system of benefits should be portable, meaning workers can move from job to job without losing their accrued benefits (such as paid time off); pro-rated, meaning that benefit contributions would be proportionate to income earned; and universal, meaning that all workers have access to them, regardless of industry or whether or not they are in traditional employment.⁶⁷ The goal of experimenting with portable benefits models at the state or local level should be to inform future national policymaking by learning more about what modern workers in new arrangements need, what models work, what types of benefits can be effectively offered or provided, price and cost sensitivity for workers and businesses, and more.

Some models of portable benefits already exist, both in the US and abroad. For example, a *Multiemployer Plan* pools benefits across multiple employers, with the package of benefits and the level of employer contributions collectively bargained between the employers and a union or group of unions. New York’s *Black Car Fund* provides workers compensation benefits to “Black Car” for-hire drivers through a 2.5 percent surcharge on each ride, paid by the rider. The *Ghent System* provides many Nordic workers with unemployment insurance financed by taxes and business contributions and administered by a third party, often a trade union. *Group Insurance* provides a suite of benefits to members of an association or

⁶⁷ Auguste et al 2015. “Common ground for independent workers: Principles for delivering a stable and flexible safety net for all types of work.” Medium. 9 November. <https://medium.com/the-wtf-economy/common-ground-for-independent-workers-83f3fbcf548f#.wcbx5f59w>

union – for example, the Owner-Operators Independent Drivers Association offers a group short-term disability plan to its members. *Secure Choice Retirement Plans* would be set up by the government (usually a state) and funded by worker contributions – workers lacking a retirement account are automatically enrolled, though they can opt out.

None of these models is perfect, providing either a narrow set of benefits or only covering a narrow group of workers. Multiemployer Plans are portable, but only within an industry, and while they sever the link between a specific employer and worker, they are nonetheless not available to independent workers. The Black Car Fund is available to independent workers, but only within a specific industry and geographic area. The Ghent system is fully portable, but relies on a strong union presence that this country lacks. Group Insurance is restricted to members of organizations that must meet certain conditions: for example, it must hold regular meetings, collect dues, and generally exist for purposes other than simply offering benefits. Finally, the Secure Choice model is simple, portable, prorated, and universal, but it involves a degree of government involvement that some may view undesirable.⁶⁸

With the increase in contingent work across the economy – and many workers looking for more flexible options for earning primary or secondary income – support for the idea of portable benefits has been growing, and several specific proposals have been floated. R-Street has proposed “Worker-Controlled Benefits Exchanges,” which would be a centralized hub for unemployment or wage insurance, paid leave, workers compensation, and other benefits. Workers would choose the plans and fund them with their own pretax contributions.⁶⁹ Nick Hanauer and David Rolf have proposed a Shared Security System, which is analogous to Social Security but would offer all of the benefits traditionally offered through employment.⁷⁰ Steven Hill builds on the existing Multiemployer Plan model with his proposal for Individual Security Accounts.⁷¹ These accounts would allow multiple employers to contribute to the benefits of a single contract employee via existing state and federal safety net programs.

Moreover, the traditional suite of benefits may not be appropriate – or enough – for contingent and independent workers. Unemployment insurance, for example, does not easily apply to a worker that is not technically employed and largely chooses when he or she works and does not work. Other benefits related to income volatility – rather than employment status – or short-term savings may be more appropriate for workers in non-employment arrangements. Similar incongruities between non-employment status and traditional benefits design can be noted about other offerings such as paid time off and family or medical leave, or even less common benefits like wage insurance.⁷²

For example, in a recent policy brief for the Aspen Institute’s *Future of Work Initiative: Fresh Perspective Series*, Jonathan Gruber of MIT proposed the creation of Security Accounts

68 Rolf, Clark, and Bryant 2016. “Portable Benefits in the 21st Century: Shaping a New System of Benefits for Independent Workers.” The Aspen Institute Future of Work Initiative. <https://www.aspeninstitute.org/publications/portable-benefits-21st-century/>

69 Lehrer 2016. “The future of work.” National Affairs. Summer. <http://www.nationalaffairs.com/publications/detail/the-future-of-work>

70 Hanauer and Rolf 2015. “Shared Security, Shared Growth.” Democracy Journal of Ideas. Summer. <http://democracyjournal.org/magazine/37/shared-security-shared-growth/>

68 Hill 2015. “New Economy, New Social Contract.” New America. August. <https://www.newamerica.org/economic-growth/policy-papers/new-economy-new-social-contract/>

72 For more ideas on how the current safety net could be updated to meet the needs of contingent workers, see the Future of Work’s Fresh Perspectives Series. This includes papers by Felicia Wong and Susan Holmberg at the Roosevelt Institute, James Capretta at the American Enterprise Institute, Jonathan Gruber at MIT, and Derek Khanna and Cesar Conda, former Congressional and White House policy staffers. <https://www.aspeninstitute.org/programs/future-of-work/fresh-perspective/>

for workers. The government would contribute to these accounts six cents for each dollar earned, regardless of the structure of the employment arrangement, up to a maximum of 6.5 weeks of current wages, after which the match would accrue to a retirement account. Funds from the Security Account could be used for a major reduction in earnings, on the job injury, disability, family or medical leave, and significant medical bills.⁷³ David Laibson at Harvard has proposed a similar savings vehicle: a share of current contributions to a worker's 401(k) would instead be deposited into a short-term savings account (i.e. a rainy day account), and once the account reached three months of income the contributions would revert back to the 401(k).⁷⁴

20. Modernize the Tax Code to Better Serve On-Demand Workers

POLICY GOAL: To make sure on-demand and other independent workers pay neither too little nor too much in taxes.

BACKGROUND: While the on-demand economy may be relatively new, the tax code is not. The last time Congress rewrote the tax code was 30 years ago, and while changes have been made on the margins, the underlying structure is basically the same.

The economy has changed a lot since then, and the tax code is showing its age. There are now over \$1.2 trillion in tax breaks in the code. A recent study by the IRS shows that the tax system is failing to collect over \$400 billion a year in taxes that it is owed, and a significant portion of this “tax gap” is attributable to non-filing and underreporting by small businesses and independent contractors. In fact, about half of the net tax gap is under-reported pass-through business income, small corporation income, and the self-employment payroll tax.⁷⁵

A recent study by American University's Kogod Tax Policy Center warns that the rise of on-demand work could exacerbate this problem. One key feature of tax code compliance is duplication: for example, when a company pays an employee wages, both the company and the employee report how much the latter was paid. But this is not always the case for independent contractors and other non-employee workers who earn less than \$20,000 from payments made by credit cards. For decades, companies that hired independent contractors had to file a 1099-MISC form if their payments exceeded \$600 annually, but the introduction of the 1099-K form in 2008 meant that companies did not have to report these payments unless they exceeded \$20,000 – a threshold under which two-third of on-demand workers fall. Kogod surveyed self-employed individuals who had earnings from on-demand work and found that more than 60 percent did not receive any 1099 tax form from their platform, which suggests that the platform was also not reporting their income to the IRS.⁷⁶ In addi-

73 Gruber 2016. “Security Accounts as Short Term Social Insurance and Long Term Savings.” The Aspen Institute Future of Work Initiative. Fresh Perspective Series. September. <https://www.aspeninstitute.org/publications/gruber/>

74 Olson and Wessel 2015. “Harvard's David Laibson wants to tweak 401(k) plans to help soften the blow of recessions.” The Brookings Institute. September. <https://www.brookings.edu/2015/09/30/harvards-david-laibson-wants-to-tweak-401k-plans-to-help-soften-the-blow-of-recessions/>

75 Committee for a Responsible Federal Budget 2016. “IRS Loses \$400 Billion Per Year in Unpaid Taxes.” The Bottom Line blog. 16 May. <http://crfb.org/blogs/irs-loses-400-billion-year-unpaid-taxes>

76 Bruckner 2016. “Shortchanged: The Tax Compliance Challenges of Small Business Operators Driving the On-Demand Platform Economy.” American University, Kogod School of Business, Kogod Tax Policy Center. May. <http://www.american.edu/kogod/news/upload/shortchanged-caroline-bruckner-kogod-au.pdf>

tion, IRS research shows that if independent workers don't receive a 1099 form, they are significantly less likely to properly report their income to the IRS.⁷⁷

This, of course, could happen if a worker is trying to avoid paying taxes. But it could also happen if on-demand earners aren't aware that they need to report their earnings to the IRS. As more traditional workers transition to independent contract work, the Kogod study reports that many have little experience with filing as a small business, which is what the tax code treats them as, rather than an employee. Indeed, one-third of on-demand workers in the Kogod survey responded that they didn't know whether they were required to make estimated quarterly tax payments.

This outcome is not just bad for the government's coffers, it's bad for the workers. Failing to pay taxes can expose these workers to potential audit and tax penalties. The confusion and complexity surrounding how to file taxes as an on-demand worker is itself a burden to them, even if they eventually figure out how to file correctly.

The complexity of the code, combined with their inexperience in filing as small businesses, could actually result in on-demand workers paying *too much* in taxes. While the tax code provides many tax benefits to small businesses, the Kogod survey found that nearly half of on-demand workers were unaware of these business deductions, expenses, or credits.⁷⁸

PROPOSAL: First, Congress should direct the IRS to conduct a rigorous survey to determine the tax compliance of on-demand workers and whether they take advantage of the small business tax provisions that are available to them. Second, Congress should direct the Treasury Department's Office of Tax Policy to undertake a comprehensive study of the current tax withholding and reporting system to identify how it should be updated to reflect the growing numbers of independent contractors, with one goal being to make tax administration more compatible with on-demand workers, independent contractors and other non-employee workers. Developing this research and requesting Treasury make policy recommendations is fundamental to informing Congress on how to close the tax gap and ease compliance burdens on small business owners.

One example of a policy proposal that Treasury should review is whether platforms should be required to withhold income for federal income taxes or subject those earnings to reporting. When income is neither reported nor withheld, over 60 percent of that income is misreported, but withholding income drops the misreporting rate down to 1 percent.⁷⁹ This would have the added benefit of ensuring workers who do not understand their tax liability will not end up surprised on tax day when they have to pay not just income tax but both sides of the payroll tax as well.

Moreover, the tax code is long due for a full rewrite. Congress should attempt to create a tax code with a broader base and lower rates, and it should do this by closely evaluating the cost and effectiveness of every tax incentive in the code. This does not preclude considering

⁷⁷ Committee for a Responsible Federal Budget 2016.

⁷⁸ Bruckner 2016.

⁷⁹ Committee for a Responsible Federal Budget 2016.

new tax incentives for work, such as those introduced in this policy agenda. We believe that the available evidence suggests that these proposed incentives would indeed be worth their cost, but ultimately they should be subjected to the same rigorous evaluation as existing tax incentives.

21. Partner with Industry to Create a Voluntary, Skills-Based Credentialing System

POLICY GOAL: To give workers control of their skills development by creating a market for training.

BACKGROUND: A well-functioning labor market requires that workers, trainers, and employers are able to effectively communicate to each other their needs and capabilities. Employers must be able to communicate the skills they're looking for, both so trainers know how to design their programs and workers know which training programs to pursue. Workers, on the other hand, need to be able to communicate the skills they have, and know that the training they pursue will lead to the recognition of additional skills.

There is substantial evidence that the U.S. labor market does not perform well in this regard. Employers can't find the talent they need, workers are unclear what skills they should be learning, and training programs have difficulty determining what skills training they should be providing.⁸⁰

Other countries solve these problems by establishing a common vocabulary. A system of credentials that are standardized across employers, industries, and occupations can make it easy for workers, trainers, and employers to recognize the supply and demand for specific skills and adjust accordingly. The U.S., however, lacks such a system for many occupations.⁸¹

PROPOSAL: Experiment with encouraging industry associations to build, monitor, and test for industry-recognized credentials. The government should help develop public-private partnerships to conduct research on occupational standards and on the best mechanisms for auditing and testing to ensure the credibility of the standards. In doing so, the partnerships should draw on standards developed in other countries. Similar proposals have been made by Robert Lerman in a paper for the National Academy of Sciences and Alexei Monsarrat in a paper for the Atlantic Council.^{82 83}

22. Reform Pell to Better Support Continuing Education

POLICY GOAL: To support worker access to mid-career continuing education by tailoring

80 Rework America 2015. "America's Moment: Creating Opportunity in the Connected Age." W. W. Norton & Company, 2015

81 Lerman 2015. "Are Employers Providing Enough Training? Theory, Evidence and Policy Implications." Prepared for the National Academy of Sciences Symposium on the Supply chain for Middle-Skill Jobs: Education, Training, and Certification Pathways, June. http://sites.nationalacademies.org/cs/groups/pgasite/documents/webpage/pga_168146.pdf

82 Ibid.

83 Monsarrat 2013. "Training Our Future: Skilled workers and the Revival of American Manufacturing." Atlantic Council, Global Business and Economics Program. December. <http://www.atlanticcouncil.org/publications/reports/training-our-future-skilled-workers-and-the-revival-of-american-manufacturing>

the Pell Grant program to the needs of older students.

BACKGROUND: Since the early 1970's, Pell Grants have played an important role in expanding access to higher education by providing tuition assistance to low-income students. The program was designed specifically for students coming out of high school to continue their general education at a four-year college prior to starting their careers.

The Pell Grant program continues to serve this population of students. But it is also increasingly serving a second population of students that are older, no longer dependent on parents, and have different educational and career goals. In the early 1980s, less than a quarter of Pell recipients were 25 or older, and roughly 40 percent were independent; in 2010, nearly half were 25 or older and almost 60 percent were independent. In fact, Pell Grants have become the primary source of grant funds for adults seeking to enhance their workforce skills.⁸⁴

This older population of students has different needs and faces different challenges. In contrast to their younger counterparts, older Pell recipients are looking for a shorter skills-based education to prepare for specific occupations rather than a four-year bachelor's degree.⁸⁵ Older recipients are also more likely to drop out: within six years of enrolling, about half fail to earn a degree or certification and are no longer enrolled, compared to just over a third of younger students.⁸⁶ The current system for determining a student's need, which is designed to measure the ability of parents to pay for their child's education, is also poorly designed for older recipients that are usually independent of their parents.

PROPOSAL: The College Board's Rethinking Pell Grants Study Group recommends splitting this program into two separate types of grants – Pell Grant Y and Pell Grant A.⁸⁷ While Pell Grant Y would operate much like the current Pell Grant program, Pell Grant A would be better tailored to the specific needs and circumstances of the older population it serves.

Specifically:

- Older students could qualify based on a simple income threshold based on the last three years of earnings. This would replace the more complicated needs analysis formula, which is unnecessary because older students are rarely dependent on their parents.
- Older students that recently lost a job of three years or more for no cause would be allowed to qualify for the program with only one year of low earnings. This would allow older students who are permanently dislocated to rapidly transition to a new career.
- Older students could use Pell funds at their own pace. While the Study Group also recommends allowing younger students this option, it is more important for older

⁸⁴ Rethinking Pell Grants Study Group 2013. "Rethinking Pell Grants." The College Board, Advocacy and Policy Center. April. <http://media.collegeboard.com/digitalServices/pdf/advocacy/policycenter/advocacy-rethinking-pell-grants-report.pdf>

⁸⁵ Ibid.

⁸⁶ Ibid.

⁸⁷ Ibid.

students that are likely balancing work, family, and school.

- Students would receive academic and career advising from an independent third party to help them select the best field of study. Choosing the right program is significantly more important for older students, for two reasons. First, most college majors provide career flexibility, while occupational education may be only relevant to specific jobs. Second, credits are generally transferable across majors, but a student that changes occupational programs will probably lose her previously accrued credits.

23. Reform Occupational Licensing

POLICY GOAL: To improve economic opportunities for independent workers by cutting regulatory red tape.

BACKGROUND: Occupational licensing is a form of regulation that requires workers to obtain the permission of the government to perform certain types of work. Licensing is common for a wide variety of occupations, including dentists, lawyers, and physicians, but in the last few decades the number of occupations that require licenses has increased dramatically. At the state level, which accounts for the majority of licensing activity, occupations requiring licenses have increased from 5 percent of the workforce in the 1950's to 25 percent today.⁸⁸ Including federal and local licensing, a total 29 percent of workers are currently licensed. While roughly a third of this growth is due to the economy becoming more service-oriented (service occupations are more likely to require licenses), two-thirds of this increase is attributed to policy decisions that have applied license requirements to more and more occupations.⁸⁹

There are, to be sure, situations in which occupational licensing is appropriate. Nearly all economic transactions involve some level of imperfect information, in which consumers cannot be certain about the quality of the good or service they are purchasing. Imperfect information can cause consumers to spend less than they otherwise would, which leads to forgone economic activity and less wealth creation. At its extreme, a significant gap in information between the consumer and the seller can cause a downward spiral in quality, leaving high- and middle-quality goods and services without a market on which to be traded.⁹⁰

Imperfect information is usually solved by competition. Consumers, either through iterated purchases or the experience of other consumers (i.e. business reputation), can usually determine to a sufficient degree the quality of a service without requiring the provider to have a specific license. But in some markets, it is necessary for the government to certify the provider. For example, if determining the quality of service requires specific expertise that most consumers lack, or if the cost of purchasing low-quality service can be dangerous,

88 Kleiner and Krueger 2013. "Analyzing the Extent and Influence of Occupational Licensing on the Labor Market." *Journal of Labor Economics*. April. <http://archive.hhh.umn.edu/people/mkleiner/pdf/Final.occ.licensing.JOLE.pdf>

89 The White House 2015. "Occupational Licensing: A Framework for Policymakers." July. https://www.whitehouse.gov/sites/default/files/docs/licensing_report_final_nonembargo.pdf

90 Akerlof 1970. "The Market for 'Lemons': Quality Uncertainty and the Market Mechanism." *The Quarterly Journal of Economics*. August. <https://www.iei.liu.se/nek/730g83/artiklar/1.328833/AkerlofMarketforLemons.pdf>

occupational licensing can be appropriate.

But there is evidence that occupational licensing has spread to far more occupations than can be justified by imperfect information concerns. In fact, studies fail to show a consistent linkage between occupational licensing and quality or safety. The White House Council of Economic Advisors surveyed 12 studies of occupational licensing and found that “empirical research does not find large improvements in quality or health and safety from more stringent licensing,” while the Goldwater Institute finds that “In truth, the health and safety justification rarely holds up under scrutiny.”^{91 92} This evidence suggests that many covered occupations, such as masseuses, cosmetologists, florists, and auctioneers, provide services that consumers are perfectly capable of evaluating themselves, with little health risk.

Meanwhile, there is a significant downside to applying occupational licensing requirements to more occupations than necessary. Licensing usually requires extensive education and training, as well as hefty fees. The Institute of Justice surveyed 102 occupational licenses and found that they required, on average, \$209 in fees and nine months of education and training.⁹³

Occupational licensing also disproportionately impacts low-income and self-employed workers. These licensing requirements can lead to lower rates of entrepreneurship among low-income workers, suggesting that they represent significant obstacles to these workers.⁹⁴ And a larger share of self-employed workers have licenses compared to employed workers, despite the fact that obtaining a license can be a greater burden because they lack employers who may sponsor the cost – and provide paid time off – for seeking a license.⁹⁵ These requirements can also require in-state education, which can restrict the ability of low-income workers to take full advantage of distance learning programs that offer low-cost and flexible options.

Occupational licensing also inhibits workplace flexibility and business model innovation. Technology is revolutionizing distance work – for example, by providing health services through telehealth centers. But because occupational licenses tend to vary state-to-state, these work arrangements are hampered by the need to obtain a license in every state serviced.

As alternative work arrangements become more common, it is increasingly vital that government not unnecessarily restrict the entrepreneurship opportunities of American workers. New independent work opportunities are more easily and efficiently accessed today than ever before, but while the barriers to entry have lessened in the ability to offer services and find and connect to customers, licensure requirements remain a significant policy barrier.

PROPOSAL: Federal, state, and local governments should review and reform their occupa-

91 The White House 2015.

92 Slivinski 2015. “Bootstraps Tangled in Red Tape: How State Occupational Licensing Hinders Low-Income Entrepreneurship.” Goldwater Institute. February. https://goldwater-media.s3.amazonaws.com/cms_page_media/2015/4/15/OccLicensing-Kauffman.pdf

93 Carpenter, Knepper, Erickson, and Ross 2012. “License to Work: National Study on Burdens from Occupational Licensing.” Institute for Justice. May. <http://ij.org/report/license-to-work/>

94 Slivinski 2015.

95 According to White House 2015, licensed workers are more likely to be self-employed than other workers, with sixteen percent of licensed workers report being self-employed as compared to 13 percent of unlicensed workers.

tional licensing requirements to ensure that they are only applied to occupations in which there is a significant market failure relating to information uncertainty, public safety, and health, and are not unnecessarily burdensome.

The Council of Economic Advisors recommends a collection of best practices, including:⁹⁶

- Consider using less restrictive systems, such as voluntary certification or registration.
- Minimize the burdens to workers of acquiring a license.
- Ensure that the substantive requirements of acquiring a license are well-tailored to quality and consumer protection.
- Explore the role that consumer rating and other reputational mechanisms can play in protecting consumers absent license requirements.
- Consider automatic formal cost-benefit analyses when regulations are enacted (sunrise review) and after they have been in place for some time (sunset review). These reviews could be conducted by commissions that are insulated from political interference and whose judgement would automatically go into effect unless overturned by the legislature.

24. Use the On-Demand Economy to Help and Encourage Unemployed Americans to Return to Work

POLICY GOAL: To help and encourage unemployed safety net recipients to return to work.

BACKGROUND: There is a substantial body of research regarding the positive effects of employment on mental health and happiness.⁹⁷ Moreover, those who are unemployed will instead rely on social safety net programs, creating a burden on taxpayers and potentially crowding out public investments. It is clear that public policy should promote work.

One obstacle for the unemployed finding work is that searching for a job takes time, focus, and a tremendous amount of effort. This can be a particular challenge for workers with specific disabilities that allow them to do some jobs but not others.

Another obstacle is that some aspects of the current safety net discourage work.^{98 99} Earning additional income causes many safety net programs to phase out – for example, a parent with two children in Connecticut that moves from poverty-level income to 150 percent of poverty will actually be worse off because the loss of benefits and additional taxes would be greater than the entire increase in income.¹⁰⁰

The on-demand economy can provide a solution. On-demand platforms serve two pur-

96 Ibid.

97 Khanna and Conda 2016 provide an overview of this literature.

98 Maag, Steuerle, Chakravarti, and Quakenbush 2012. "How Marginal Tax Rates Affect Families at Various Levels of Poverty." National Tax Journal. December. <http://www.urban.org/sites/default/files/alfresco/publication-pdfs/412722-How-Marginal-Tax-Rates-Affect-Families-at-Various-Levels-of-Poverty.PDF>

99 Moffitt 1992. "Incentive Effects of the U.S. Welfare System: A Review." Journal of Economic Literature. March. http://www.unc.edu/~shanda/courses/plcy289/Moffitt_Incentive_Effects_Welfare_System.pdf

100 Maag, Steuerle, Chakravarti, and Quakenbush 2012.

poses: they seamlessly connect workers with jobs, and they collect and display reputation data, which can serve to allay concerns about hiring people without an in-person meeting and potentially replace the interview process. The result is that more jobs than ever are at workers' fingertips.

Moreover, the large number of options in the sharing and on-demand economy makes it easier for workers to find jobs tailored to their specific skills and abilities, thus helping workers advance in their careers and providing more meaningful work.

We should leverage this power to help unemployed workers transition from public assistance back into work.

PROPOSAL: The federal government should study the extent that on-demand platforms have improved access to jobs for workers, with a special focus on safety net beneficiaries and the disabled. Government offices administering safety net benefits, such as the 2,500 American Job Centers, should facilitate access to on-demand jobs by maintaining an updated directory and providing access to certain resources necessary for on-demand work, such as computers. States should ensure that their unemployment insurance eligibility rules allow workers to seek part-time work. Finally, if the evidence is clear that on-demand platforms have had a significant effect in lowering barriers to employment, and that government offices are effective in moving beneficiaries to work, then work requirements should be applied to certain safety net programs as appropriate.

Specifically, the government should study how on-demand platforms have improved access to work by answering the following questions:

1. What are the skills and capital equipment that on-demand jobs require? What share of these jobs require few specialized skills and equipment?
2. What share of safety net recipients have specialized skills and access to capital goods that may be useful in doing on-demand work? What skills and equipment are they lacking that might better prepare them for on-demand work?
3. What is the geographic distribution of on-demand jobs – and specifically, low-skill and low-capital platforms – relative to the distribution of safety net recipients? Are there enough low-skill and low-equipment jobs that can be done online to compensate for geographic mismatches?

Regional offices that administer government services should also facilitate access to on-demand jobs. This should include maintaining an updated directory of local on-demand jobs (and jobs that can be done online). This directory would also include information on physical requirements, so that those classified as disabled can more easily find jobs that are consistent with their abilities.

Regional offices should also help beneficiaries get access to specific equipment necessarily for on-demand work. States should be allowed to experiment with using a portion of their unemployment funds to buy equipment to lend out to beneficiaries – purchasing a \$100 used Chromebook to put a beneficiary back on a career path may be a cost-effective investment.

Finally, if the aforementioned study finds that on-demand platforms have significantly increased access to work for current safety net beneficiaries, and if state efforts to connect beneficiaries to on-demand work through regional offices prove effective, then Congress should consider expanding work requirements to safety net programs that do not have them.

Currently, the Temporary Assistance for Needy Families (TANF) program requires that recipients spend a certain amount of time each week engaged in “work activities,” such as working, looking for work, or pursuing job training.¹⁰¹ Work requirements also exist within the Supplemental Nutrition Assistance Program (SNAP) and Section 8 Housing Choice Voucher program.¹⁰²

The argument against applying work requirements to other safety net programs is that many recipients simply don’t have access to a job, especially if they lack sufficient skills, transportation options, or live in a depressed region. This is doubly true during a recession, when there simply aren’t enough jobs to go around. Moreover, family responsibilities can make it difficult to hold down jobs with inflexible or unpredictable hours.

These are valid concerns. Work requirements should not be fully applied to the rest of the safety net until there has been sufficient research and programmatic experimentation to show that on-demand platforms can offer adequate work opportunities to a significant share of safety net recipients. Moreover, these work requirements should be deactivated during periods of severe economic downturn.

This proposal is modeled after a report authored by Cesar Conda and Derek Khanna and published in Aspen Institute’s *Future of Work Initiative: Fresh Perspectives Series*.¹⁰³

25. Promote Labor Mobility with the Unemployment Insurance Program

POLICY GOAL: To help workers return to work and find good jobs by promoting mobility and facilitating job searching.

BACKGROUND: A healthy and dynamic economic ecosystem is one where the labor market can continually readjust to the changing needs of the economy. This requires a workforce that is mobile and can be quickly retrained.

As economies grow and evolve, they rarely experience that growth uniformly. Some regions will grow quickly, others more slowly, and some will shrink. And within those trends, the mix of labor demanded in each region changes as well.

A key component of a healthy economic ecosystem is a mobile labor market where labor moves to where it is most highly needed and valued. This leads to higher wages for workers and a more productive workforce for businesses. And for many years, the labor market was

101 Center on Budget and Policy Priorities 2015. “An Introduction to TANF.” Policy Basics. June. <http://www.cbpp.org/research/policy-basics-an-introduction-to-tanf>

102 Falk, McCarty, and Aussenberg 2014. “Work Requirements, Time Limits, and Work Incentives in TANF, SNAP, and Housing Assistance.” Congressional Research Service. February. http://greenbook.waysandmeans.house.gov/sites/greenbook.waysandmeans.house.gov/files/R43400_gb.pdf

103 Khanna and Conda 2016. “Using the Gig Economy to Reform Entitlements.” The Aspen Institute Future of Work Initiative. Fresh Perspective Series. September. <https://www.aspeninstitute.org/publications/condakhanna/>

indeed mobile: the U.S. mobility rate has consistently been significantly higher than many other developed countries, and this has been pointed to as one of the factors for our relatively low historical unemployment rates relative to Europe.¹⁰⁴ From the westward expansion of the 19th century to the Great Black Migration of the 20th century, American history is a story of people moving to greater opportunity.

But in the last few decades, labor mobility has fallen.¹⁰⁵ According to Census data, from 2005-2010 internal migration was at its lowest level since at least 1940.¹⁰⁶ While there are a number of theories for why this is happening, it is clear that this could be having negative effects on workers, businesses, and the economy.

This is particularly concerning for workers. After all, as documented in this report, technology and globalization have made it easy for businesses to contract out labor if they cannot find it locally; but these factors have not provided workers with the same alternatives. Moreover, there is substantial evidence that location has a strong influence on upward mobility, which suggests that moving can increase economic opportunity.¹⁰⁷

A healthy and dynamic ecosystem also adjusts to changing skills needs. Workers who lose their jobs are perfect candidates to enter training or retraining programs, especially for new and emerging industries. Unfortunately, training and retraining programs tend to last longer than UI's conventional 26 weeks of benefits, meaning that unemployed workers must forgo income for a period of time after the benefits expire to complete the training.¹⁰⁸ Forgoing income is not an option for many workers: nearly half who lose their jobs have zero liquid wealth at the time of the job loss.¹⁰⁹

PROPOSAL: Congress should explore reforms to unemployment insurance that would promote greater labor mobility and training.

Both R-Street Institute and the Center for American Progress (in partnership with National Employment Law Project and the Georgetown Law Center on Poverty and Inequality) have proposed reforms to unemployment insurance that would promote labor mobility. R-Street has proposed mobility grants that would allow workers who lose their jobs and lack significant assets to receive their benefits in one lump sum rather than over time.¹¹⁰ The total level of benefits would be set to the amount that a worker would receive were they to remain unemployed for roughly nine months.¹¹¹

The Center for American Progress proposal would be more expansive. In addition to current benefits, recipients would receive a Job Seekers Allowance (JSA), a weekly payment to

104 Molloy, Smith, and Wozniak 2011. "Internal Migration in the United States." National Bureau of Economic Research. Working paper. August. <http://www.nber.org/papers/w17307.pdf>

105 Ibid.

106 Lehrer and Sanders 2014. "Moving to Work." National Affairs. http://www.nationalaffairs.com/doclib/20131219_LehrerSanders_Winter2014.pdf

107 Chetty, Hendren, Kline, and Saez 2014. "Where is the Land of Opportunity: The Geography of Intergenerational Mobility in the United States." Quarterly Journal of Economics. June. http://scholar.harvard.edu/files/hendren/files/mobility_geo.pdf

108 West, Dutta-Gupta, Grant, Boteach, McKenna, and Conti 2016. "Strengthening Unemployment Insurance Protections in America: Modernizing Unemployment Insurance and Establishing a Jobseeker's Allowance." Center for American Progress. June. https://cdn.americanprogress.org/wp-content/uploads/2016/05/31134245/UI_JSAreport.pdf

109 Chetty 2008. "Moral Hazard vs. Liquidity and Optimal Unemployment Insurance." National Bureau of Economic Research. Working Paper. <http://www.nber.org/papers/w13967.pdf>

110 Lehrer and Sanders 2014.

111 Ibid. Eli Lehrer and Lori Sanders of R-Street describe this as 70-80% of a year.

help offset job search costs. This allowance would be less than half the size of conventional benefits and last half as long, and would be subject to a means test.¹¹²

While the proposals are quite different – most notably, the Center for American Progress proposal would be in addition to current unemployment benefits, while the R-Street Institute proposal would simply allow recipients to front-load their benefits – they would both provide short-term income support, which would help unemployed workers relocate to find better jobs and prepare themselves for the economy of the future, and conduct a more successful job search process. Research suggests that these effects will lead to better matches between workers and businesses, resulting in higher wages for workers and greater job stability.¹¹³

112 West, Dutta-Gupta, Grant, Boteach, McKenna, and Conti 2016.

113 Caliendo, Künn, and Mahlstedt 2015. "The Return to Labor Market Mobility: An Evaluation of Relocation Assistance for the Unemployed." IZA Discussion Paper Series. July. <http://ftp.iza.org/dp9183.pdf>

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