

The Federal Role  
in  
Unemployment Compensation  
Administration

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A

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The Social Science Research Council was organized in 1923 and formally incorporated in 1924, composed of representatives chosen from the seven constituent societies and from time to time from related disciplines such as law, geography, psychiatry, medicine, and others. It is the purpose of the Council to plan, foster, promote, and develop research in the social field.

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## FOREWORD

WHEN IN 1936 a study of the administrative organization and methods of the federal-state system of unemployment organization was initiated under the Social Science Research Council's sponsorship, it was not possible to foresee fully how intricate the mechanisms required by the recently enacted statutes would prove to be. The first five years of operation have been a period of constant revision and adjustment, complicated by severe unemployment when benefits first became payable in many states, and by the process of integrating unemployment compensation and employment service functions. It was therefore found desirable to extend the duration of the project out of which the present volume has grown until a substantial degree of stability in unemployment compensation administration appeared to have been attained. Just before the termination of the study in June 1940, a new set of problems was created by the expanded labor supply responsibilities of the combined unemployment compensation and placement agencies with the beginning of the defense program. These, however, fall largely within the labor market field and its placement aspects, and have not thus far significantly affected the management of unemployment compensation in its narrower sense. These factors, therefore, are not included in the scope of the study.

Through three of the four years during which the study of unemployment compensation was in progress, developments in the states and in Washington were observed jointly by Mr. Atkinson, who had previously been on the staff of the Ohio Institute, and by Mr. Walter Matscheck, formerly director of the Civic Research Institute of Kansas City, Missouri. Their activities during the first year were part of the program of administrative studies of the social security program undertaken by the Council's Committee on Public Administration in the spring of 1936. At that time Mr. Atkinson and a group of associates were engaged upon an analysis of the closely related problems of federal-state relations in the administration of the then separate employment service. This resulted in the publication in 1938 of *Public Employment Service in the United States*.

Thereafter Messrs. Matscheck and Atkinson collaborated in detailed observations of administrative practices and policies in nearly half of the United States, including the New England, North Central, and West

Coast states as well as a number of others in the southeast and southwest. In the summer of 1937 the sponsorship of the study was taken over by the Council's Committee on Social Security. The services of both collaborators throughout 1937 and 1938, and in considerable part thereafter, were largely devoted to consultation with state and federal officials and to aiding the interchange of the experiences of these officials. Memoranda and reports of an essentially interim character were, however, prepared from time to time and resulted in two formal publications: *The Administration of Unemployment Compensation Benefits in Wisconsin* (1937), and *Problems and Procedures of Unemployment Compensation in the States* (1939).

Mr. Matscheck's active participation ended in the spring of 1939 when he became associated with the Railroad Retirement Board. Field investigation was carried further by Mr. Atkinson and it is he who has prepared the text of this report, though it is at most points a distillation of the observations and analyses of both participants in the undertaking.

The study has been focused upon issues concerning possible improvements in administrative operation or structure. Although many suggestions are made for changes in the unemployment compensation systems as they now exist, these suggestions have been developed primarily in terms of strengthening administration without detailed discussion of their social and economic implications. It is recognized that matters have been dealt with which are still highly controversial, including the relative desirability of a federal-state as against a national method of managing unemployment compensation, the effects of certain types of experience rating, and the further development of national standards under the present federal-state system.

On these points and other points, it should be emphasized that while the study has been sponsored by the Committee on Social Security it has not been submitted to the Committee or to the Social Science Research Council for formal review or approval. The Committee has regarded it as its responsibility to make certain that the studies which it sponsors are based upon ample first-hand investigation so that the investigator will acquire full knowledge of all relevant data and factors, and to satisfy itself that the author of a report has considered thoroughly all aspects of any controversial questions with which he may find it necessary to deal. In the end, however, the statements and conclusions of the author are entirely his own and do not purport to express the opinions or attitudes of the Committee or of the Social Science Research Council.

An especial acknowledgment is made by Mr. Atkinson to the careful observations, critical insight, and breadth of view which Mr. Matscheck contributed during his collaboration, and to the cooperation and courtesy with which he was aided by the unemployment compensation agencies and officials of both the state and federal governments. He also acknowledges gratefully the untiring and capable assistance of Maude Klock, who was his secretary throughout the study, and the aid given by Julia Henderson in summarizing materials relating to the Social Security Board's function in the federal-state unemployment compensation system. The volume was prepared for publication by Mary Charles Cole of the Committee's staff.

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FEDERAL ROLE  
IN UNEMPLOYMENT COMPENSATION



## CHAPTER I

# THE FEDERAL-STATE SYSTEM OF UNEMPLOYMENT COMPENSATION

THE AMERICAN SYSTEM of unemployment compensation is unique not only in its size and in many of its insurance features, but also in the form and complexity of its administration. With two exceptions compulsory unemployment insurance laws in other parts of the world are administered by a single agency for the entire country.<sup>1</sup> Ours, however, is not a national system of unemployment insurance. In a sense perhaps it should not even be termed a system, but a patchwork of fifty-one state and territorial insurance schemes within a national frame provided by the Social Security Act.<sup>2</sup> There are numerous differences among states in matters of detail; the payroll taxes levied for unemployment compensation purposes vary somewhat in coverage and in the computation of rates, and the benefits paid differ in method of determination and in relative adequacy. Yet the basic pattern is much the same throughout the country. The combination of state plans constitutes a distinct system of unemployment insurance, national in scope though fundamentally different in nature from that of any other country. It is, in brief, a federal-state enterprise, based on fifty-two state and federal laws enacted by as many legislative bodies and administered by an even greater number of state or federal agencies.

The unemployment compensation program also presents an innovation in federal-state relations within the United States. Contrary to established practice, the Social Security Act provides for federal grants to cover the entire expense of the states in administering unemployment compensation. Except for certain emergency activities at the bottom of the depression, this is the only example of federal assumption of the full

<sup>1</sup> In Switzerland unemployment insurance is administered by the cantons under a federal law providing for partial financing by the federal government. Norway has a locally administered system with national grants to make up deficits in local funds. The state of Queensland, Australia, has established unemployment insurance, but since there is no dominion participation, administration is concentrated in a single agency for the entire area affected.

<sup>2</sup> 49 *Stat. L.* 620 (1935). Amended by 53 *Stat. L.* 1360 (1939). At many points in this and subsequent chapters the word "state" is used to include Alaska, Hawaii, and the District of Columbia, which are covered by the Social Security Act and which, with the forty-eight states, make up the fifty-one jurisdictions having unemployment compensation.

cost of a state-administered undertaking. Through the medium of grants-in-aid, the federal government in the last thirty years has cooperated extensively with states in financing and developing a number of services of national interest; but these grants have nearly always been contingent upon substantial state participation in the cost—usually on an equal matching basis.

Federal grants have tended to overcome the traditional separation of state and national administration and to bring about a cooperative relation, often termed a partnership, in the conduct of the activities concerned. With federal grants have usually gone a generous measure of technical advice and a limited amount of supervision. When the federal government takes over the entire cost of administration, however, as it has with unemployment compensation, its influence and supervision almost inevitably undergo a great expansion. As in any partnership, the one who supplies the capital may be expected to have the controlling voice. Instead of holding the position of an equal, the state tends to become the agent and the federal government the principal in such an arrangement. In continental Europe, state and local governments have long been used as administrative agents of the national government. But in the United States, this relationship—which seems implicit in the present financing of unemployment compensation administration—represents a fundamental change in our system of government and may have considerable significance for the future.

When the Social Security Act was in preparation, study was given the question whether social insurance should be administered directly by the national government or through the states. For old-age insurance the President's Committee on Economic Security, which formulated the legislation, recommended national administration, while for unemployment compensation it proposed a federal-state plan of operation.<sup>3</sup> The decision in favor of a federal-state system turned on several considerations. Foremost among them was the danger that a national system might be held unconstitutional by the Supreme Court. The Committee was also much impressed by the need for experimentation and adaptation to local conditions. It recognized that wage levels and the character of the industrial system differ materially in various parts of the country and that a period of trial and adjustment might be necessary to develop a plan of unemployment insurance suited to our needs, if indeed a single plan could ever be devised which would be applicable on a national basis.

<sup>3</sup> *Report of the President's Committee on Economic Security, 1935.*

Accordingly, the Committee concluded that it would be unwise to enact a uniform plan of unemployment compensation for the country and that a federal-state system would be preferable, at least in the early stages of the program.

Since the establishment of unemployment compensation, a separate federal system of unemployment insurance has been set up for railroad workers, which is administered by the Railroad Retirement Board. This study, however, focuses on the federal-state system of unemployment compensation and deals with railroad unemployment insurance only as it relates to, or reacts upon, the administration of that system.

### BASIC CONSIDERATIONS

A few basic facts merit attention at the outset in examining the unemployment compensation system. The first is that the Social Security Act, though it laid the foundation for unemployment compensation, did not itself create the system. In line with the recommendations of the President's Committee, the Act aimed mainly at "removing the obstacles to State action" and providing a few essential safeguards.<sup>4</sup> The principal obstacle to which the Committee had reference was the fear of placing local industries at a competitive disadvantage by the imposition of the state taxes necessary for financing unemployment benefits. This difficulty the Social Security Act removed by levying a federal payroll tax against which employers might credit their payments to state unemployment compensation funds up to 90 per cent of the federal tax. Thus, the federal tax equalized the burden on employers in states with and without unemployment compensation levies and practically forced the states to adopt unemployment compensation in order to avoid the loss of revenue available to them for the support of such a program. The extraordinary effectiveness of this device in stimulating state action is demonstrated by the fact that, by two years from the passage of the Social Security Act, all the states had enacted the necessary legislation.<sup>5</sup>

A second basic fact is that the form of the unemployment compensation system is determined almost entirely by the states. Though the Social Security Act imposes a few requirements, the states have wide discretion as to both the substantive and the administrative provisions of

<sup>4</sup> *Ibid.*, p. 13.

<sup>5</sup> Seven states enacted unemployment compensation laws before the passage of the Social Security Act, but all of these except Wisconsin passed their laws in 1935 after the enactment of federal legislation was considered a foregone conclusion.

their laws. The coverage of the system, the type of reserve fund, the benefit structure, and the administrative organization are fixed for each state by its own legislation. The Social Security Act allows the states to choose among a pooled fund plan, a pooled fund with experience rating, an individual employer reserve account system, a guaranteed employment plan, or a combination of these schemes, and to devise their own methods for computing benefits and benefit duration. States are free to require workers as well as employers to contribute to the support of the system. They may institute a stamp plan for the collection of the payroll tax or rely on periodic reporting and payment. Likewise, benefits may be uniform for broad classes of workers, as in Great Britain, or proportioned to previous earnings, as in American workmen's compensation systems. In fact, the conditions of the Social Security Act are so broad and the undertaking so new and unexplored that the full scope of state discretion and the possible range of experimentation and variation cannot adequately be indicated. Nevertheless, it is significant that with few exceptions the state unemployment compensation laws conform closely to a single basic pattern.

Another fundamental consideration is the close relation of unemployment compensation and employment service. In nearly all countries these two functions are conducted by a single agency as a unified undertaking. While such integration did not originally exist in the United States, it is rapidly taking place. From the beginning the public employment offices were used by the unemployment compensation system in dealing with claimants. Now, the two functions are administered by the same departments or agencies in both state and federal governments. Unified administration of employment service and unemployment compensation is necessary for the protection of the insurance system and for the convenience of the unemployed worker, who is more interested, as a rule, in obtaining employment than in securing benefits. Not only does employment service afford a means of shortening unemployment and reducing the drain on the compensation reserves, but it provides the only practical method of applying a work test to prevent malingering. Foreign experience has demonstrated the necessity of such a test and shown that the chief means of making it effective is the offer of jobs through a public employment office.

In consequence, the unemployment compensation system has been built around the public employment offices. At the local level its administration is now so inextricably interwoven with that of employment

service that it is impossible to separate the two. In recognition of this relationship, the term "employment security" has been coined in the United States to embrace both functions and has been applied to the agencies administering them.

### THE ADMINISTRATIVE PATTERN

The administration of unemployment compensation involves action on three administrative levels. On the national level, the work is concentrated mainly, though not wholly, in the Social Security Board and is performed largely through its Bureau of Employment Security. In the states, employment security agencies are of several types. Twenty-one states have assigned unemployment compensation and employment service to the department of labor, industrial commission, or other agency charged with the enforcement of state labor laws, while another has placed them in its treasury department. Most of these states have created a single bureau within the department or commission to administer the two functions. Twenty-nine jurisdictions have established independent agencies for employment security administration, in five headed by a single director and in the others by a commission.<sup>6</sup> Most of these commissions are part-time bodies which function through executive officers, but a few are full-time boards which exercise direct control over operations. Normally, the state employment security agency consists of an unemployment compensation division, an employment service division, and a number of units to look after internal administration and render legal, informational, and research and statistical service.

In spite of the close relation between them, unemployment compensation and employment service require rather different types of operating machinery. Employment service is a highly decentralized undertaking. The local employment office is the heart of the service, as it is in the community that jobs are found and workers placed. The central office of an employment service requires only a handful of supervisory and technical personnel even in the more populous states. On the other hand, unemployment compensation, as administered in the United States, is a relatively centralized function. The worker files his benefit claim and reports at the local employment office; but the collection of the payroll

<sup>6</sup> In two of the twenty-nine states the agency administering unemployment compensation is nominally in, but not subject to control by, the department of labor, and in a third state it is in a so-called department of social security which does not exercise administrative authority over it.

tax, the maintenance of the wage records from which his benefits are computed, the determination of his claim, and the recording and payment of his benefits are all carried on by the central office. Hence, most of the personnel of the employment service are at the local level, while the greater part of the staff of the unemployment compensation system are in the central office.

The local organization for employment security administration consists of some 1,600 full-time employment offices and about 3,000 part-time offices and contact points periodically visited by itinerant interviewers working out of the regular offices. These part-time offices and contact points are constantly changing with local fluctuations in unemployment and in placement opportunities. The unemployment compensation system also uses the mails in serving workers in some of the more remote and sparsely settled areas, especially in the Rocky Mountains and the Far West.

Together the state agencies administering the employment security program had on August 31, 1940 a personnel of about 35,000. In addition, the Social Security Board had about 850 employees assigned to the employment security program.

In the year ending June 30, 1940—the first in which all states paid benefits—the administrative expenditures of the state agencies amounted to \$65,550,000, but it is impossible to separate unemployment compensation and employment service costs. Of this sum, \$3,345,000 was financed from federal grants for employment service under the Wagner-Peyser Act, \$3,390,000 from state and local funds for matching these grants, and the remainder, \$58,815,000, from unmatched grants under the Social Security Act for both unemployment compensation and employment service. The total expenditure represented 6.8 per cent of the proceeds of the payroll taxes collected by the state and federal governments for unemployment compensation. In Great Britain, where unemployment insurance has been in effect for thirty years, the cost of administering unemployment insurance and employment service has ranged in recent years between 6.3 and 9.3 per cent of the contributions collected by the unemployment insurance system.<sup>7</sup> In making comparisons, however, it should be remembered that the public employment office is a much older institution and plays a much larger role in the

<sup>7</sup> Because of differences both in organization and methods and in contribution and benefit scales, only a rough comparison of the administrative costs of the British and the American unemployment insurance systems is warranted.

labor market in Great Britain than in the United States. On the other hand, it is reasonable to expect the administrative expenses for unemployment compensation to decline somewhat as the undertaking becomes better established and its operations perfected.

### MAGNITUDE OF UNEMPLOYMENT COMPENSATION OPERATIONS

Taking the country as a whole, about 28,000,000 workers are covered by the unemployment compensation system, but of them several million who have had excluded as well as covered employment are insured on the basis of only a part of their earnings. Under the procedure generally followed, a separate earnings record must be kept at the central office of the state agency for each worker covered. This means for the entire country the maintenance of 28,000,000 employee wage records.

Approximately 810,000 employers are subject to state unemployment compensation taxes. During the year ending June 30, 1940, employers paid \$810,000,000 to state unemployment compensation funds, and employees in six states contributed about \$44,000,000, making a total of \$854,000,000. The state agencies maintain for each liable employer an account showing contributions paid under the payroll tax. In states with experience rating the agencies also keep a record of the unemployment experience of each employer as a basis for computing tax rate adjustments.

In the year 1939-40, the fifty-one employment security agencies received 10,900,000 initial claims for benefits and made 46,550,000 benefit payments aggregating \$482,500,000. The average weekly payment for total unemployment was \$10.50. It is estimated that about 5,000,000 persons received benefits. Each new claim received at the central office of an agency required a determination of the worker's eligibility and, if eligible, the computation of his benefit rate and duration. For every person receiving benefits, an account had to be carried showing all payments made.

From this description it is evident that the administration of unemployment compensation involves accounting and record-keeping operations of immense proportions. While there are many complex problems of procedure, some of which have by no means been solved, the difficulties experienced in the conduct of unemployment compensation arise more from the magnitude and the sharp fluctuations of the work load than from the intricacy of the tasks to be performed. Most of the operations are relatively simple and routine, but those having to do with

benefit claims, determinations, and payments demand rapid handling and the ability to adjust promptly to a highly variable and often unpredictable operating load.<sup>8</sup>

During the initial years of a program so large and lacking in precedent, it is inevitable that the machinery should creak at times. That it has performed its function with few serious breakdowns, even in a period of severe unemployment, and at a cost comparing favorably with that of countries with well-established systems of unemployment insurance is to the credit of the state and federal personnel who have launched the undertaking. At its inception many students of unemployment insurance questioned the practicability of the American plan of unemployment compensation; some were outspokenly critical. The answer is, it has been and is being operated with reasonable success in most areas though many secondary problems remain to be solved. With further study and experience, operating efficiency can be greatly increased. Among the tasks ahead, probably the most important are improvement of the system of administration, elimination of some basic inadequacies of the benefit structure, extension of the coverage, and strengthening of the employment service. This study deals particularly with the first two.

<sup>8</sup> The Appendix presents a brief summary of the principal substantive features of the unemployment compensation system.



## CHAPTER II

### ORGANIZATION AT THE FEDERAL LEVEL

THE UNEMPLOYMENT COMPENSATION activities of the federal government are divided between two major departments or agencies, and nearly a dozen bureaus or offices are involved in some degree in their administration. While the principal responsibilities are vested in the Social Security Board of the Federal Security Agency, important duties are assigned to the Treasury Department with respect to the fiscal aspects of the program.

#### TREASURY DEPARTMENT

The Treasury Department has as its role the administration of the federal unemployment tax and the custody and management of the unemployment trust fund in which the states must deposit their unemployment compensation reserves. The federal unemployment tax is levied at the rate of 3 per cent on the payrolls of employers having eight or more workers in insured employment, but actual collections are normally limited to one-tenth of this rate by the operation of the 90 per cent credit or offset allowed employers on account of their contributions to state unemployment compensation funds.<sup>1</sup> This payroll tax must be clearly distinguished from the one imposed by the federal government to finance old-age and survivors insurance, which is not subject to offset and is applied without regard to the number of workers.

The Bureau of Internal Revenue in the Treasury Department administers both of the payroll taxes levied for the social security program, as well as the tax on railroad companies for old-age annuities to railroad workers. Together, payroll taxes now comprise one of the chief sources of federal revenue, and their collection constitutes one of the major functions of the Bureau. The federal unemployment tax is payable in January of each year on the basis of the previous year's payrolls. The tax returns and payments are filed with the collectors of internal revenue in the field, but the record work is largely concentrated at the central office of the Bureau in Washington.

<sup>1</sup> The provisions relating to the federal unemployment tax originally formed Title IX of the Social Security Act, but are now incorporated in the Federal Unemployment Tax Act passed in 1939. 53 *Stat. L.* 1387.

Though the Bureau of Internal Revenue and the state employment security agencies operate independently in the collection of payroll taxes, the administration of the federal unemployment tax brings them into relation at two points. First, the state agencies must annually certify to the Bureau the names of employers contributing to state unemployment compensation funds and the amount of payroll reported and tax paid by each. This information is checked by the Bureau to discover delinquent employers and is compared with the federal returns to verify the credits claimed by employers for the payment of state taxes under the 90 per cent offset provision.

The second point of interrelation between federal and state administration is less direct. In determining the liability of employers under the federal tax, the Bureau of Internal Revenue has developed a considerable body of rulings interpreting the coverage provisions of the federal act. While these rulings are not binding upon the states in the interpretation of the corresponding provisions of their own laws, they exert a very important influence upon state decisions. There has been a marked tendency for state agencies to follow the precedents of the Bureau in the application of their laws where the state provisions are similar to the federal and even in some cases where they are not.

The Social Security Act and the Federal Unemployment Tax Act both require the prompt deposit of state unemployment compensation receipts in the unemployment trust fund in the federal treasury.<sup>2</sup> This fund was created and its administration vested in the Treasury Department mainly to safeguard unemployment compensation reserves against loss by poor investment and to lessen the danger of the money market being upset by the operation of fifty-one separate reserve funds. The states make their deposits with the trust fund through Federal Reserve Banks and member banks serving as federal depositories. On receipt into the treasury, a deposit is credited to the state's account in the fund and invested in federal securities. For convenience the Treasury Department invests the fund in special securities bearing interest at the average rate for outstanding federal obligations. At present this rate is 2½ per cent. The states may draw upon their accounts in the trust fund whenever money is needed for the payment of benefits.

In effect, the Treasury Department acts as the banker for the states in

<sup>2</sup> Section 303(a) of the Social Security Act (49 *Stat. L.* 626) and section 1603 of the Federal Unemployment Tax Act (53 *Stat. L.* 1391). Section 904 of the Social Security Act establishes the unemployment trust fund and governs its administration.

the administration of their reserve funds. Several subdivisions of the Department participate in the operation of the trust fund, especially the offices of the Commissioner of Accounts, the Treasurer of the United States, and the Commissioner of the Public Debt; but the work is largely absorbed into the regular operation of these units and requires very few full-time employees. As compared with state operation of fifty-one reserve funds, the present arrangement undoubtedly effects a substantial saving in administrative expenses and affords greater protection to the funds.

### SOCIAL SECURITY BOARD

The employment security program, of which unemployment compensation is a branch, is one of three broad programs under the supervision of the Social Security Board. Two of these—employment security and public assistance (including old-age assistance, aid to the blind, and aid to dependent children)—are carried on by the states with federal grants by the Board, and the third—old-age and survivors insurance—is administered directly by the Board for the entire country. The last requires the maintenance of a federal organization numbering nearly 9,000 employees, whereas the Board's staff for the other two programs consists of around 1,300 persons. The relative complexity of the Board's problems, however, is not measured in any sense by the size of the federal personnel engaged in the three undertakings. In fact, a federal-state program may present more difficult problems for a federal agency than a federally administered enterprise and, in the case of unemployment compensation, probably does.

#### *Functions of the Board*

As set forth in the federal legislation, the functions of the Social Security Board with respect to unemployment compensation are few. They may be summarized under six heads:

(1) Determination of the conformity of state unemployment compensation laws (including regulations and interpretations as well as the statutes themselves) to the requirements of the Social Security Act and the Federal Unemployment Tax Act, and periodic certification thereof to the Secretary of the Treasury to establish the eligibility of states for grants and of employers for the 90 per cent offset against the federal tax.<sup>3</sup> Most

<sup>3</sup> These requirements are set forth in section 303(a) of the Social Security Act (49 Stat. L. 626) and sections 1602 and 1603 of the Federal Unemployment Tax Act (53 Stat. L. 1388).

of these requirements are reasonably specific and do not raise particularly fundamental issues for the Board.<sup>4</sup> From the standpoint of the Board's influence over the administration of the unemployment compensation system, the most important requirements are those of section 303(a) of the Social Security Act, which stipulates that state laws shall include provisions for:

"(1) Such methods of administration (including after January 1, 1940, methods relating to the establishment and maintenance of personnel standards on a merit basis, except that the Board shall exercise no authority with respect to the selection, tenure of office, and compensation of any individual employed in accordance with such methods) as are found by the Board to be reasonably calculated to insure full payment of unemployment compensation when due; . . .

"(6) The making of such reports, in such form and containing such information, as the Board may from time to time require, and compliance with such provisions as the Board may from time to time find necessary to assure the correctness and verification of such reports; . . .

"(8) Effective July 1, 1941, the expenditure of all moneys received pursuant to section 302 of this title [i.e., grants for administrative expenses] solely for the purposes and in the amounts found necessary by the Board for the proper and efficient administration of such State law; and

"(9) Effective July 1, 1941, the replacement, within a reasonable time, of any moneys received pursuant to section 302 of this title, which, because of any action or contingency, have been lost or have been expended for purposes other than, or in amounts in excess of, those found necessary by the Board for the proper administration of such State law."

The first of these provisions affords the legal basis for personnel standards and some other administrative regulations laid down by the Board. The second (paragraph 6) enables the Board to require reports and prescribe reporting procedures. The last two specifically sanction the imposition of detailed federal restrictions upon the use of money granted for administrative expenses.

(2) Authorization of grants in "such amounts as the Board determines to be necessary for the proper and efficient administration" of state unemployment compensation laws.<sup>5</sup>

(3) Determination, after notice and opportunity for hearing, that a

<sup>4</sup> The requirements of the federal acts are summarized on pages 36-38.

<sup>5</sup> 49 *Stat. L.* 626, sec. 302(a) as amended by 53 *Stat. L.* 1378.

state in administering its law is failing to comply substantially with the requirements of the federal acts. Such a determination renders the state ineligible for the benefits afforded by the particular provision of the federal law the conditions of which have not been met.<sup>6</sup>

(4) Determination, after notice and an opportunity for hearing, that in a substantial number of cases there has been a denial of unemployment compensation to individuals entitled thereto under the state law. Such a finding stops federal payments for state administrative expenses.<sup>7</sup>

(5) Approval of the payment of compensation through agencies other than public employment offices.<sup>8</sup>

(6) Study and recommendation of legislation and administrative policies concerning unemployment compensation.<sup>9</sup>

In addition, the Board administers the Wagner-Peyser Act, relating to employment service.<sup>10</sup> Since employment service and unemployment compensation are financed and operated as a joint enterprise, the functions of the Board under this law have an important bearing upon the administration of unemployment compensation as well. The Wagner-Peyser Act authorizes annual grants to the states for employment service, but much the greater part of the cost of this service is financed from funds provided under the Social Security Act. The Wagner-Peyser Act, however, confers upon the Board broad authority to prescribe minimum standards for state employment services. It also requires the Board to maintain national placement services for veterans and farm workers and an employment office for the District of Columbia.<sup>11</sup>

The actual role of the Social Security Board in the unemployment compensation system is not adequately indicated by a summary of the functions vested in it by the terms of the Social Security Act. In practice, its part has been much larger and its influence much greater than the language of the Act implies. In passing upon the conformity of state laws to the terms of the federal act, the Board has been able to mold state legis-

<sup>6</sup> 49 *Stat. L.* 627, sec. 303(b) and 53 *Stat. L.* 1388, secs. 1602, 1603.

<sup>7</sup> Payments are also halted by a finding of the Board that the state is failing to make its records available to the Railroad Retirement Board or to cooperate with any federal agency administering an unemployment insurance law. 52 *Stat. L.* 1112, sec. 303(c).

<sup>8</sup> 49 *Stat. L.* 626, sec. 303(a)(2) and 53 *Stat. L.* 1391, sec. 1603.

<sup>9</sup> 49 *Stat. L.* 636, sec. 702.

<sup>10</sup> 48 *Stat. L.* 113.

<sup>11</sup> The functions of the federal agency under the Wagner-Peyser Act were formerly vested in the United States Employment Service in the Department of Labor and were transferred to the Social Security Board by Reorganization Plan No. I, effective July 1, 1939. The functions of the federal agency prior to this change are described in detail in Atkinson, Odenchantz, and Deming, *Public Employment Service in the United States* (Chicago: Public Administration Service, 1938), pp. 55-77.

lation on several points. To a much greater extent, however, it has shaped state laws through technical service and advice. More important, in determining grants it has subjected state budgets and operating plans to minute review and revision. In so far as administration is concerned, this practice has been the foundation of federal influence. Not only has it permitted the Board to offer suggestions while plans were still in the formative stage, but, coupled with the Board's requirement of strict adherence to the approved budget, it has enabled the federal agency to enforce its recommendations. In addition, the Board has gradually been developing a body of administrative standards with which states must comply. As these standards have been perfected and put into operation, the Board has tended to relinquish somewhat the grip which it has held upon the states through the itemization of grants.

Though mentioned only briefly in the Social Security Act, one of the major sources of federal influence and one of the principal contributions of the Board to the unemployment compensation program has been the provision of research and technical service. Most of the fundamental research in unemployment compensation and much of the more basic planning of organization and procedures have been conducted by the federal agency. To a great degree, state research and developmental work has been directed to immediate problems and to devising the detailed application of plans the broad features of which have been formulated at the federal level. A large amount of technical and installation service has been furnished state agencies in establishing and perfecting their procedures and record systems. In addition, the Board has acted as a clearing house for the dissemination of state experience.

But the importance of the Board's role in launching the unemployment compensation system must not be permitted to obscure the vital part played by the state agencies in its establishment. Most of the work necessary to make unemployment compensation a going concern has been performed by the states. The Board has provided valuable aid and guidance, but the state agencies have made the detailed preparations and set up and operated the system.

### *Organization of the Board*

The Social Security Board is virtually a department within a department. It was created as an independent executive establishment, but, by the terms of Reorganization Plan No. I, in 1939 it became a part of the

Federal Security Agency, which includes the Public Health Service, the Office of Education, the Civilian Conservation Corps, the National Youth Administration, and a few other units comprehended within the broad purpose of social welfare. In the Agency the Social Security Board constitutes not one but a constellation of bureaus under a single administrative body.

The Board itself consists of three members appointed by the President with the advice and consent of the Senate for overlapping terms of six years. Members devote full time to their duties and receive salaries of \$10,000 a year. One member is designated by the President as chairman.

As a body the Board establishes the administrative units necessary for the performance of its functions, and regulates and controls their operation. The personnel is appointed by the administrator of the Federal Security Agency on the recommendation of the Board. Each bureau of the Board is headed by a director, chosen in this manner and answerable to the Board and its executive director. The Board itself is principally a policy-determining body. Most decisions of basic policy are made by it or by administrative officers after consultation with it, and many questions of lesser importance are considered by it as well as delicate and difficult problems of state relations. Actual negotiations with the states are generally carried on by the bureaus or the executive director. The Board also takes all final actions on the approval and certification of state laws for conformity with the Social Security Act and on the grant of funds for state administration. If a formal issue of state compliance with the terms of the Act arises, the Board hears and decides the case.

In most matters the Board acts as a body. Its sessions are frequent and prolonged. Unlike many boards, the members have not parceled out the functions among themselves and do not act as administrators of segments of the program. The chairman serves in a measure as the general administrative officer of the Board, but in the main the executive director acts as the coordinator and supervisor of the administrative organization, subject to very active participation by the Board itself, considering the size and scope of the enterprise.

The affairs of the Board are conducted through three major bureaus, corresponding to the three social security programs with which it is concerned, and several staff or service units. Among the latter are the Bureau of Research and Statistics, which carries on basic research in the social security field, and the Bureau of Accounts and Audits, which keeps

the accounts of the Board and audits the administrative expenditures of state employment security and public assistance agencies. The Information Service handles the Board's publicity and advises states on public relations, while the State Technical Advisory Service works with state agencies on personnel problems and procedures, especially as they concern the merit system. The General Counsel's Office of the Federal Security Agency provides legal service for the Board and advises it on the conformity of state laws with the Social Security Act.

The Bureau of Employment Security is the principal arm of the Social Security Board for the performance of its functions relating to unemployment compensation and employment service. This bureau was created in the summer of 1939 by the merger of the former Bureau of Unemployment Compensation and the United States Employment Service, which was transferred to the Board at that time. The Bureau carries on the relations of the Board with state agencies administering unemployment compensation and employment service. It reviews and revises state plans and budgets and recommends to the Board the amount of federal grants. It conducts research on unemployment compensation and employment service problems and develops suggested legislative provisions, regulations, and operating procedures. Most of the administrative standards prescribed by the Board are formulated by the Bureau. Its staff supplies the greater part of the technical service afforded state agencies. Likewise, its representatives in the field maintain continuous contact with state operations to aid the states on their problems and keep the Bureau and the Board informed on developments in the states. Through its Employment Service Division, the Bureau also conducts the Veterans' Placement Service, the Farm Placement Service, and the District of Columbia Employment Center.

The Bureau of Employment Security consists of five divisions, one of which—the Field Division—acts as its principal agent for the conduct and coordination of state relations. This Division has charge of the field staff of the Bureau, by whom negotiations are largely handled, and serves as the channel through which most communications and transactions between the federal agency and the states flow. It issues federal standards and declarations of policy to the states and receives state requests for advice and service. Matters requiring federal approval are either disposed of by the Division or routed by it to the appropriate technical unit. But the principal function of the Division is the review of



state budgets and the formulation of recommendations on grants. In order that state problems may be handled with greater understanding, the Division is organized into four sections, each dealing with a definite group of states.

Separate divisions are maintained for unemployment compensation and employment service. With respect to the general function assigned it, each of these divisions is responsible for the study of problems and the development of principles, standards, and procedures. The Unemployment Compensation Division works on such matters as wage reporting, employer experience rating, and benefit formulas and procedures, while the Employment Service Division studies placement problems and develops aids for vocational counseling and the registration and selection of workers. Both divisions provide consulting service for the states within their respective fields. In addition to these units, the Research and Statistics Division compiles and analyzes data on unemployment compensation and employment service operations and carries on research in some of the underlying problems of both functions. The Division of Fiscal and Management Standards makes cost analyses and formulates standards of business practice for state agencies.

The Social Security Board conducts its field operations through a system of twelve regional offices. In laying out its regions the Board adhered strictly to state boundaries and gave principal consideration to three factors: convenience of transportation and communication, the basic social and economic characteristics of the different areas, and the number of workers covered by the old-age insurance system. Particular weight was accorded the last of these factors. As a result, the regions are somewhat similar in number of compensable workers but vary widely in area and in number of states contained. Region II consists of New York State alone, while Region VII includes six states in the Old South, and Region XI, with a similar number of Rocky Mountain states, extends from the Canadian border to the Mexican line.

Though the number of compensable workers is a logical consideration in dividing the country for federal administration of old-age insurance, since it measures the work load, it has proved by no means so appropriate a basis for setting up areas for the conduct of federal-state relations in a grant-in-aid program. In such a program the state is the unit and the number of states is, on the whole, a better index of size and federal activity than the number of persons insured. A federal staff operating

within a one- or even a three-state region has rather a limited opportunity to observe the enterprise and may not be able to bring to state agencies a breadth of background and experience much greater than that of the state officials themselves. On the other hand, when the federal agency maintains as minute supervision and control as in unemployment compensation, a six-state region places a severe strain on regional officials.

The staff of a regional office consists of a regional director answerable to the executive director of the Board and of regional representatives assigned by the various bureaus, together with the necessary assistants and clerical personnel. The division of authority between the regional director and the regional representatives is somewhat vague and difficult to define. In general, the regional director has charge of regional office routines and exercises limited supervision over the bureau representatives attached to his office. In so far as unemployment compensation is concerned, his role has been more that of coordination than of direction. He advises the representative of the Bureau of Employment Security on problems and provides sufficient supervision to see that Board policies are observed, that the work of the different bureaus is coordinated, and that state relations are properly conducted. He frequently participates in the more difficult negotiations and usually handles relations with governors.

With the aid of his assistants the regional representative of the Bureau of Employment Security serves as its agent in the field. He is more than the eyes, ears, and mouthpiece of the Bureau. While most matters requiring formal action must still be referred to Washington, his recommendations on state relations are to an increasing degree becoming the decisions of the Bureau. He carries on most of the direct negotiations with state agencies and advises them on federal requirements and on many of their administrative and technical problems. His major responsibility is the examination and revision of state budgets preliminary to review by the Field Division in Washington. He also passes on a variety of matters requiring federal approval and on a few types of questions gives the final answers. In addition, he keeps the Bureau informed of the needs and problems of the states and their compliance with federal requirements. In large measure the Bureau must depend on its regional representatives for a realistic understanding of the program in operation, while the states rely upon them for access to federal technical service and the experience of other agencies.<sup>12</sup>

<sup>12</sup> The following list, summarizing the principal activities of the staff in one region dur-

## MAJOR PROBLEMS OF FEDERAL ORGANIZATION

The administration of a federal-state undertaking, such as the unemployment compensation system, is complicated at best. Not only must the legal and psychological gap between federal and state agencies be bridged—often at no mean expenditure of time, patience, and diplomacy—but a considerably larger number of officials must be brought into cooperation and a much greater amount of administrative red tape must be unwound than in an enterprise entirely administered by either federal or state authorities. For this reason, simple, clear-cut organization is especially essential on both federal and state levels.

### *Coordination of Federal Agencies*

One of the major problems of organization experienced at the federal level in the administration of unemployment compensation has been that of coordination. Nothing is more damaging to federal prestige and influence in a grant-in-aid program than conflicting or inconsistent federal action. It may either arouse the ire of state officials or invite shrewd efforts to take advantage of federal ineffectiveness. In either event it tends to undermine federal-state relations and impair the efficiency of administration. The problem of coordination has arisen both among the units of the Social Security Board and between the Board and other federal agencies concerned with unemployment compensation, but inter-agency coordination has presented the greater difficulties.

Prior to the summer of 1939, the development of both unemployment compensation and employment service was seriously hampered by the separation of the federal agencies responsible for them. Though the two

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ing a two-month period in 1939, gives a fair indication of the nature of the work of the regional representative and his assistants:

1. Review and revision of state budgets, including a budget hearing in each state.
2. Approval of transfers within the approved budget for the current period.
3. Recommendation to the Bureau of actions which should be taken on expenditures disallowed by the federal auditors.
4. Authorization of out-of-state travel by state personnel.
5. Examination of state operating reports and inspection of state agencies as a basis for suggesting improvements and for judging budget requirements.
6. Arranging with the Bureau for the services of a specialist to aid one state in working out new partial benefit procedures.
7. Transmittal and interpretation to the states of new federal policies and regulations.
8. Preparation of monthly reports on the status and problems of each state agency.
9. Obtaining information requested by the Bureau or seeing that the states provided it directly on request.
10. Transmittal of Bureau reports to the states and of required state materials to Washington.

functions were carried on locally through public employment offices—largely by the same personnel—and were administered by the same state agencies, the funds for their support were derived partly from the Social Security Board and partly from the United States Employment Service in the Department of Labor. In consequence, the state agencies had to present their plans and budgets to two federal bureaus and comply with two sets of federal policies and requirements to obtain their grants.

Though the two bureaus eventually instituted a procedure for joint conduct of state relations, it proved but a cumbersome makeshift. The bureaus continued to differ in their views on the organization of state agencies—one striving for integration and the other for a dual form of organization—and on budget and personnel procedures as well as on the relative emphasis to be given the two functions. Conflict at the federal level engendered rivalry and friction between unemployment compensation and employment service officials in the states and impeded the development of both undertakings. Happily, this episode has been closed by the consolidation of the federal bureaus under the Social Security Board, but the services have not yet entirely overcome the handicap of this early strife.

The separation of the tax and the insurance aspects of unemployment compensation in the federal government also creates problems of coordination. These problems relate mainly to employer coverage under state and federal payroll tax provisions and to the exchange of information on liable employers. Differences between federal and state rulings on coverage tend to confuse employers and react on state agencies. If the Bureau of Internal Revenue holds an employer or a class of employers exempt, the states are apt to be subjected to pressure to grant a similar exemption. It is not surprising, therefore, that they tend to follow the lead of the Bureau in the interpretation of coverage provisions.

This condition derives its main significance from the facts that decisions on employer coverage also affect the insurance status of workers and that the Bureau of Internal Revenue is a tax, rather than an insurance, agency. It naturally views the federal payroll taxes primarily from the revenue standpoint. In administering the many taxes for which it is responsible, it is forced to weigh the cost of collection against the revenue yield and to apply its resources where they will produce the greatest return, even though this may have an unfortunate effect on the social insurance benefits of some classes of workers, particularly those employed by very small employers. Hence, the need for close collaboration be-

tween social insurance agencies and the Bureau. In practice, however, there has been little consultation on the interpretation of coverage between Internal Revenue authorities and the unemployment compensation officials either of the Social Security Board or of the state agencies. The principal effort at coordination has been the publication by the Board of a bulletin service on state and Internal Revenue rulings.

In the administration of payroll taxes the Bureau of Internal Revenue and the state employment security agencies are performing similar tasks and dealing with substantially the same groups of employers. The need of cooperation is apparent so long as separate administration of payroll taxes continues. Yet little has been done to explore or work out the possibilities of cooperation and clearance of information on liable employers and their payrolls.

While the coordination needed in the administration of payroll taxes involves both federal and state operations, it could be achieved more readily if all federal aspects of the social security program, including the payroll taxes, were administered by the Social Security Board. In the states the administration of the payroll tax is a function of the employment security agency rather than the tax department. Similar integration on the federal level would assure the dominance of the social insurance viewpoint in the determination of coverage and the enforcement of the tax and would simplify the development of needed cooperation between federal and state agencies in the administration of payroll taxes. On the other hand, there are important advantages in the collection of payroll taxes by the Bureau of Internal Revenue. This plan avoids the necessity of establishing a second federal system of collection offices and revenue agents and no doubt reduces administrative costs. It also brings to the social insurance system the experience and prestige of the Bureau of Internal Revenue in the collection of taxes. Furthermore, the concentration of tax records and investigation work in a single agency makes readily available the valuable information obtained in the administration of other federal taxes for use in the enforcement of payroll taxes.

It may well be that closer cooperation and greater clearance of information between the Bureau of Internal Revenue on the one side and the Social Security Board and the state agencies on the other would be preferable to transferring the administration of federal payroll taxes to the Social Security Board. The problem merits further study. Another possibility would be to transfer to the Board the responsibility for issuing

regulations and hearing appeals on employer coverage. Such an arrangement would bring the interpretation of the coverage provisions under the insurance agency, which is the appropriate body to exercise this authority in a social insurance program; but it would separate the adjudication of coverage issues from the application of the rulings in the field. Whatever the plan, more adequate appropriations are needed for investigation and follow-up to make the coverage provisions fully effective.<sup>13</sup>

### *Unified Conduct of State Relations*

A second organization problem encountered by the Social Security Board has been the development of a single channel for the conduct of relations with state employment security agencies. Prior to 1939 each unit of the Board dealt directly with the states on matters which fell within its field of activity. Three divisions of the Bureau of Unemployment Compensation (now the Bureau of Employment Security) carried on direct relations with state agencies and sent members of their staffs into the field. Likewise, the Bureau of Research and Statistics, the Bureau of Accounts and Audits, the General Counsel's Office, and the State Technical Advisory Service had personnel in the field visiting states. An effort was made to coordinate these disjointed operations by a central clearance of mail, but with only limited success. States were annoyed by overlapping requests for information and inconsistent advice and instructions and were confused by the multiplicity of federal units with which they had to deal. The number of persons sent into the field on limited missions created heavy travel expenses for the Board and encroached unduly on the time of state officials.

This experience plainly demonstrated the necessity of greater integration within the Board and of concentrating the conduct of state relations in a single unit. This was accomplished early in 1939 by transferring certain units to the Bureau of Unemployment Compensation and setting up a Field Division within that Bureau to carry on negotiations and handle the review of budgets, about which state problems tend to cluster. This Division was given supervision of the regional staff of the Bureau and was made the clearance point for contacts between other units and the states on technical problems.

<sup>13</sup> Satisfactory coordination has already been achieved between federal and state employment security agencies and the Treasury Department in the handling of funds. Some troublesome problems, however, have arisen in working out the needed coordination between the railroad unemployment insurance system and the unemployment compensation system.

The new arrangement has demonstrated its desirability. It enables the states to deal with the regional representative and the Field Division on most federal-state business and to obtain prompter and more consistent federal action. It has reduced waste motion for the Board and the Bureau and resulted in better informed handling of state relations. The principal criticism of the plan has been that it might cut off the technical units from the flow of technical problems from the field and result in less adequate service to the states. This danger, though not unreal, can be minimized by clearance procedures and clear-cut policies on matters to be referred to the other divisions and by supervision to see that the staff of the Field Division uses their services on problems falling within their spheres of special competence. Obviously, a new state benefit procedure should be reviewed by the technical person specializing in that particular field rather than by a person dealing mainly with administrative questions. Similarly, a statistical problem belongs to the Research and Statistics Division rather than the Field Division. There are cases, however, which concern both divisions because of their budgetary implications or effects on federal-state relations.

Centralization of state relations has its greatest value and necessity in dealing with administrative problems and questions having important administrative implications. It should not deprive the technical personnel of first-hand contact with state operations and the questions received from the field, but rather should provide a more orderly procedure for bringing the technical resources of the federal agency to bear upon state problems.

### *Decentralization of Authority to Regional Offices*

The degree to which authority should be decentralized to regional offices has presented a third problem of special difficulty for the federal agency. In the first year the personnel of the Bureau of Unemployment Compensation operated directly from headquarters, and decisions were entirely centralized in Washington. At this stage in the enterprise a high degree of centralization was inevitable because of the lack of national policies and experienced personnel. The process of decentralization began with the establishment of regional offices late in 1936 and the assignment of Bureau representatives to the regions. The next important step was the introduction of a regional review of state budgets preliminary to examination in Washington. Early in 1939 came the permanent assignment of most of the budget analysts to the field. Since then

there has been a gradual increase in regional activities and responsibilities and a slow expansion of the field staff. Yet by the summer of 1940 it had reached a total of only about 45 persons.

As the regional personnel has gained familiarity with state agencies and as federal policies have crystallized, the Bureau of Employment Security has placed increasing reliance on its field staff in the conduct of state relations. Very little power of decision, however, has actually been transferred to the field. In the spring of 1939 the Bureau announced that it was about to transfer to the regional offices the decision of all questions covered by established federal policies, but no such sweeping decentralization of authority has occurred.

The principal advantages of decentralization of administrative authority to the regions are that it permits prompter action and makes for better informed and more realistic handling of state problems. It avoids the necessity of long-range negotiation and complicated clearances, which slow down transactions between the states and the central office of the Bureau. At the same time it places authority in the regional representative, who has a detailed acquaintance with local conditions and the needs of state agencies. He is in a position to discuss issues directly with state officials and obtain first-hand information on which to base federal action. In general, state administrators appreciate the opportunity for such discussion and are more willing to trust the judgment of a person close to the operating scene than of one a thousand miles away. Greater decentralization of authority is almost universally desired by state employment security officials and is backed up by many examples of what they—and often the regional representatives—consider inappropriate action by the Bureau in Washington. The volume of these cases has, of course, been much increased by the minuteness of the controls exercised by the federal agency and the large number and frequent insignificance of the questions which have had to be referred to the Bureau. It is not easy to determine in Washington the exact number of desks and chairs that should be purchased in Texas or Montana or the number of interviewers needed by an employment office in California.

Against decentralization have been urged the greater difficulty of developing and maintaining uniform national policies and the danger that divergent and perhaps ill-advised action in the regions might lessen the Bureau's effectiveness or lead to controversies with the states. Obviously, the transfer of authority to the regions would necessitate close supervision of regional operations. Another objection is the broader back-



ground of the central staff and the ability of the central office to bring to bear on problems nation-wide experience and more specialized and expert personnel. The regional staff is necessarily small and its horizon more or less limited to the few states with which it works. Furthermore, the central office is less subject to state pressure and in a better position to make independent and impartial judgments. The regional representative is sometimes too near the scene and too much a part of the state agency to handle troublesome issues satisfactorily. After all, he has to live with the agencies in his region, and he may acquire the agency point of view. On the other hand, the very closeness of his relations with state officials often enables him to dispose of delicate issues that might readily arouse hard feeling and resistance. For example, the adoption of the merit system, as required by Board standards, has been greatly facilitated by the ability of regional directors and representatives to deal with governors and agency officials on a friendly, informal basis.

Even if unemployment compensation were administered as a national system, a large amount of authority would have to be assigned to regional officials for efficient operation. The area served is too vast and the fluctuations in volume of activity too violent for centralized administration. Even in the British and German unemployment insurance systems there has been considerable devolution of authority to district or regional offices. While in the United States the division of responsibility between state and federal governments provides most of the decentralization needed, the extent of federal participation in the unemployment compensation program makes desirable some decentralization of power within the federal agency. How far it should go depends upon the minuteness of the controls exercised by the federal agency over the states. The more detailed the controls, the greater is the decentralization needed.

Under the present system of federal supervision of state agencies, it would seem that, within the bounds of established national policies, the regional office might well be empowered to decide all except the most difficult and fundamental questions arising with states and those requiring specialized technical attention. Matters such as the approval of budget transfers, salary adjustments, leases, and equipment purchases—if the requirement of federal approval is retained—could be turned over to the regions. The review of legislation and regulations for conformity with the social security laws, however, requires highly specialized personnel and uniformity of decision; hence, it appropriately belongs in the

central office, though this need not prevent the regional staff from giving informal advice on these matters. The detailed examination and revision of state budgets could be left to the regions, subject to a general review by the central office.<sup>14</sup> Direct negotiation with the states is obviously a regional function except on questions of extraordinary difficulty and importance or of a highly technical nature. Likewise, the inspection of state agencies and the less specialized types of service to states fall within the province of the regional staff.

The role of the central office in a decentralized plan of operation would include substantially the following principal responsibilities: the determination of national standards and basic policies; the supervision of the work of regional offices through inspection and review to see that national policies are followed and the work is competently performed; a general review of budgets, as revised by the regions, for the same purposes and to check comparative costs; the review of state laws, regulations, etc., for conformity with the Social Security Act; the maintenance of research and developmental activities; the provision of specialized technical service to the regions and the states; and the conduct of comprehensive surveys and special studies of state operations for the purposes of rendering constructive service to the states, obtaining information for central office studies, and determining the effectiveness of state agencies and the regional offices.

This division of responsibility between central and regional offices would reduce the flow of routine administrative problems into the central office and would permit it to concentrate more on important questions of policy and on research and technical service. The staff required by the central office would consist mainly of a small group of administrators, well acquainted with the entire program and particularly conversant with federal-state relations, and a considerable body of technical specialists for research and developmental work and for surveys and consulting service.

Only a small degree of specialization is feasible in the regional staff of the Bureau, but within the limits of size it is desirable. The regional representative must be an all-round man. His major responsibilities, and the ones to which he devotes most of his own time, relate to state negotiations and matters of administration, particularly organization, personnel, and finance; yet he meets all types of questions arising in state agencies, including the most technical. To perform his function, the

<sup>14</sup> Budget procedure will be discussed in Chapter V.

regional representative needs, and in several regions now has, the assistance of at least one person familiar with the problems and procedures peculiar to unemployment compensation and another specializing in employment service, who can effectively appraise state operations and advise the states on all except the more intricate questions falling within their fields. So long as the Bureau requires federal approval of minute transactions, something can be said for apportioning the work among the regional personnel according to states. In the long run, however, functional specialization within the regional staff should provide more expert supervision and more constructive service to the states. In an enterprise as diverse and complex as the employment security program, it is not reasonable to expect many to master the entire field. Only by functional specialization can the federal staff bring to the program a knowledge and experience materially greater than that of the state personnel with which it deals. As a rule, the work of the Bureau in the regions probably cannot be broken down beyond administration, unemployment compensation, and employment service; the more highly specialized service will no doubt have to be obtained through the central office, as it is at present.

### CHAPTER III

## FEDERAL INFLUENCE UPON STATE LEGISLATION

UNEMPLOYMENT COMPENSATION affords a striking example of federal influence on state legislation. A comparison of state laws at the beginning of benefit payment reveals an astounding similarity, not merely in the general insurance plan, but also in the detailed provisions and in the language used. The fact is that the states depended almost entirely upon the Social Security Board for technical assistance in the preparation of their unemployment compensation legislation. Under the circumstances, they had little alternative but to do so. They had to enact laws before January 1, 1937 to avoid the loss of more than \$250,000,000 of revenue available to them for unemployment compensation in the first year under the 90 per cent offset provision of the federal unemployment tax.<sup>1</sup> As the Social Security Act was not signed until August 14, 1935, there was less than a year and a half in which to adopt the necessary legislation. Because of doubt concerning the constitutionality of the federal law and the political uncertainties of a presidential year, most states deferred legislative action until after the 1936 election.<sup>2</sup> Then there were less than two months in which to qualify under the tax offset provision. Obviously, there could be little study of unemployment compensation problems at that juncture. The main concern was to enact a law before December thirty-first.

But even if there had been time for study, most states would have had to rely heavily upon the Social Security Board. Unemployment compensation was a highly technical subject on which there was no American experience. In many states there probably was no one who had given it serious consideration or could claim familiarity with its problems. The task of formulating the legislation and educating state officials concerning it, therefore, fell squarely upon the Social Security Board. At no

<sup>1</sup> All but 15 of the 51 jurisdictions covered by the Social Security Act had passed unemployment compensation laws by December 31, 1936. The remaining states enacted legislation in the first half of 1937. Congress subsequently turned over to them 90 per cent of the federal tax collected in 1936 with respect to employment within their jurisdictions. (Public Act No. 353, 75th Congress)

<sup>2</sup> Many states had created committees or assigned legislative draftsmen to undertake the preparation of bills before the fall of 1936. As a rule, these committees or legislative agents obtained drafts from the Social Security Board and adhered rather closely to them.

stage in its existence have the responsibilities and the influence of the federal agency been so great as at the very inception of the program.

### THE DRAFT BILL

The Social Security Board prepared what it termed not a model but a draft bill and developed a small staff of specialists to assist state officials and committees in formulating unemployment compensation measures. Since the Draft Bill forms the basis of most of the unemployment compensation legislation of the country, it merits attention.

#### *Preparation and Influence*

The preparation of a state unemployment compensation bill was undertaken by the President's Committee on Economic Security from plans and actuarial estimates made by its technical staff. These plans were based upon studies of European unemployment insurance experience and American workmen's compensation systems, influenced considerably by the legislation already passed in Wisconsin<sup>3</sup> and a comprehensive study made in Ohio.<sup>4</sup> Early in 1935 the Committee released preliminary drafts of its bill in the hope that many states would enact legislation during the regular sessions of that year. Owing to the delay in the passage of the Social Security Act, however, only a few states adopted unemployment compensation laws at that time. Upon its creation in August 1935, the Social Security Board took over part of the staff of the President's Committee and continued the study of legislative problems. In January 1936 it issued the first Draft Bill complying with the legislative requirements of the Social Security Act.<sup>5</sup> This bill was considerably revised and elaborated in the course of the year, and new editions were brought out in the fall and the following winter.<sup>6</sup>

The Draft Bill, particularly the revision published in January 1937, provided the model for most of the state laws and amendments adopted before benefits became payable. A number of states accepted it almost

<sup>3</sup> The Wisconsin Act was passed in January 1932. (*Laws of Special Session of 1931-32*, Chapter 20)

<sup>4</sup> *Report of the Ohio Commission on Unemployment Insurance, 1932.*

<sup>5</sup> Social Security Board, *Draft Bills for State Unemployment Compensation of Pooled Fund and Employer Reserve Account Types*, January 1936. The Draft Bill was prepared in two forms, one providing for a pooled fund plan and the other for an employer reserve account plan. The two bills differed only in the sections dealing with these features. For convenience, they have generally been referred to as the Draft Bill. That term will be used throughout this discussion, but it should be understood to embrace both plans.

<sup>6</sup> *Ibid.*, revised editions of September 1936 and January 1937.

in toto with the insertion of the necessary provisions to fit the administrative organization and procedures of the state. In most states large parts of the law were copied verbatim from the Draft Bill. In fact, the most striking differences in state legislation as it existed in 1938 reflected mainly the adoption of different options and the use of different editions of the Draft Bill rather than departures from its provisions. The Bill provided for either a pooled fund plan—with or without employer experience rating—or an employer reserve account plan. Also, it contained an optional provision for employee contributions and alternative forms of administrative organization, as well as some lesser alternative features. Some of the details were left blank to be filled in by the state, such as the number of workers required to make an employer subject to contributions and the maximum number of weeks for which benefits would be paid. Prior to 1939, most of the differences in state laws related to such matters or to detailed phraseology.<sup>7</sup>

The most controversial issue in the enactment of unemployment compensation laws was the choice between the pooled fund and the employer reserve account plans. In a number of states the latter was strongly urged by employer groups, while organized labor insisted upon the former. The pooled fund plan with experience rating was accepted as a satisfactory compromise in most states. In general, labor desired a broad coverage including employers with less than eight workers, whereas employers preferred to limit coverage to that of the federal unemployment tax. There also was some demand from employers that employees be required to contribute, but this was usually opposed by labor and was seldom adopted.

Apart from such issues, on which the Social Security Board was officially neutral, the most important variations in state laws related to the method of calculating benefits. The early editions of the Draft Bill based the duration of benefits for the individual worker upon the number of weeks of employment he had had in the preceding two years (one week of benefits for four weeks of work up to a stipulated limit). They also provided for a benefit rate of one-half his full-time weekly wage computed by multiplying his hourly wage rate by his full-time weekly hours as determined from a detailed record of his weekly earnings and hours of employment. To reduce the record-keeping and reporting work for employers and to simplify the operation of the state agencies,

<sup>7</sup> Many of the respects in which states departed from the standard pattern are indicated in the Appendix summary of state insurance plans.

an entirely different scheme was devised in the fall of 1936 which based benefits upon quarterly earnings and permitted employers to report once a quarter on the total earnings of each worker instead of reporting on hours and earnings, week by week. The states which passed laws early in 1936 adopted the former method, but most of them later amended their acts to substitute the second plan.

### *Revision of the Draft Bill*

Aside from the change in the benefit formula, the revisions of the Draft Bill in the early years represented chiefly refinements and elaborations. The definition of employment was improved to incorporate more definite rules for determining when an employer-employee relation exists and to reduce gaps and duplication in coverage in the case of persons working in more than one state or for establishments located in a state other than that where the work is performed. Some further modifications were devised relating to the benefit formula and eligibility for benefits. Changes were also made in some of the provisions on experience rating, seasonal unemployment, and a few other features of the Bill.

A few months' experience in the payment of benefits demonstrated the need for drastically simplifying benefit formulas and procedures. Twenty-two states started the payment of benefits in January 1938 in the midst of one of the sharpest declines in employment in the history of the country. As a result, the unemployment compensation system was subjected to an unexpectedly severe test at the beginning of benefit operations. The impracticability of the existing complex method of computing benefits was soon apparent. Workers could not understand the process, and the agencies could not handle claims promptly and accurately. Accordingly, the Social Security Board instituted a study looking to the simplification of the system. As soon as they were able to extricate themselves from the avalanche of claims and benefit payments, the state agencies likewise began giving serious attention to the revision of their laws. Out of these studies came a series of proposals for the simplification of the benefit formula and the eligibility requirements. These changes were incorporated in the Draft Bill and adopted with variations by many of the states in 1939.<sup>8</sup>

<sup>8</sup> Social Security Board, *Simplification of the Benefit Formula in State Unemployment Compensation Laws*, February 1939. Another plan of simplification which was partially adopted in several states was presented in Walter Matscheck and Raymond C. Atkinson, *Problems and Procedures of Unemployment Compensation in the States* (Chicago: Public Administration Service, 1939).

It is significant that there was not the general acceptance of federal proposals in 1939 as in previous state legislation. By this time state administrators had gained a better understanding of unemployment compensation and had begun to have their own ideas on how the system could be perfected. Furthermore, outside groups had become better informed and more vocal. In consequence, 1939 saw the adoption of several proposals definitely contrary to the views of the federal agency and the beginning of a trend toward diversity as against the previous tendency toward uniformity in state legislation.

#### TECHNICAL SERVICE TO THE STATES

During the period when states were enacting their unemployment compensation laws, the small technical staff of the Social Security Board cooperated actively with state committees in the formulation and presentation of bills. The Board offered its aid to governors in preparing legislation. While it was the policy of the Board to work with and through official agencies wherever possible, in some states where official interest was lacking it dealt with private groups which had taken the initiative in seeking legislation. Usually those sponsoring unemployment compensation legislation called upon the Board for a draft or submitted bills to it for examination. As a rule, a member of the federal staff was sent into the state for a short time to go over the bill in detail and to aid in working out revisions deemed desirable by the federal agency. In many cases, federal representatives appeared before legislative committees to explain the measure. The task was primarily one of education. State committees and legislative draftsmen lacked the understanding of unemployment compensation necessary to avoid technical errors which might have serious consequences. Moreover, some provisions, especially the benefit formula, were so intricate that only the initiated could properly explain them and indicate the reasons for their various features.

It has sometimes been charged that the federal agency attempted to dictate the form of state legislation. This statement, however, presents a distorted picture of the situation. The facts were that the states were confronted with a new and involved legislative problem with which they had to deal within a short period of time. Under the circumstances, they badly needed and usually sought such technical assistance as the Board could offer. The small size of the federal staff and the large number of



legislatures taking action in the closing weeks of 1936 necessitated hasty review of proposals and usually limited to the minimum the assistance the Board could afford any one state.

Nevertheless, the situation enabled federal representatives to exercise a very important influence over the legislation enacted. In advising states, it was but natural for them to recommend the types of provisions currently deemed most desirable by the Board and its technical staff. On a few issues on which the Board took no official position, the staff, through correspondence and personal contacts, undoubtedly tilted the balance in favor of the views of the federal agency. It is significant, for example, that, though either the pooled fund or the employer reserve account plan would have met the requirements of the Social Security Act and employers evinced considerable interest in the latter scheme, only one state other than Wisconsin adopted it exclusively<sup>9</sup> and only five provided for it in combination with the pooled fund plan.<sup>10</sup> Where there was strong interest in the employer reserve account system, it is but fair to say that the pooled fund plan with experience rating was commonly suggested as a preferable alternative. In some cases, it is probably also true that federal influence was thrown on the side of broad coverage. For obvious reasons, the federal agency tried to dissuade states from including provisions making their laws inoperative if the Social Security Act were held unconstitutional.

In general, the efforts of the federal staff were directed to obtaining sound and workable state legislation within the bounds of the information then available, and to clearing up errors and omissions which might lessen the effectiveness of the unemployment compensation system. On a few points—notably the provision on the appointment of the personnel of the unemployment compensation agency—foresight during the legislative period has materially aided the Board in seeking improvements in administration. The original Draft Bill provided for the appointment of personnel on a “non-partisan merit basis,” and a later revision, for appointment “on the basis of efficiency and fitness as determined by . . . examinations.” These provisions, which were accepted by most of the states along with other features of the Draft Bill, have proved very useful in bringing pressure for the establishment of merit systems for state agencies. On the other hand, some widely copied provisions of the Draft Bill have since risen up to plague their authors. Notable examples

<sup>9</sup> Nebraska. Wisconsin adopted the employer reserve account plan in 1932.

<sup>10</sup> Indiana, Kentucky, Oregon, South Dakota, and Vermont.

are the requirement of coordinate divisions of unemployment compensation and employment service and some of the cumbersome features of the benefit formula and of the experience rating plan.

After the initial period the policies of the Board on legislative service changed in several respects. Since the creation of state unemployment compensation agencies, it has dealt almost exclusively with them on legislative problems and left to them the responsibility of defending or opposing amendments. Now it rarely sends out legislative specialists from Washington. Negotiations on legislation are carried on either by correspondence or through the regional representative or the attorney stationed in the regional office. The regional representatives advise state agencies on legislative problems, but seldom appear before legislative committees and then only upon request. The Bureau of Employment Security continues to maintain a very small staff specializing on these problems. They advise the states and the field personnel of the Bureau on legislative questions and develop amendments to meet new requirements of federal law and effect improvements in the unemployment compensation system.

State agencies are asked, but not required, to submit their legislative proposals to the Bureau for review before introduction and to send in copies of other unemployment compensation bills likely to receive serious consideration. This practice enables the Bureau to point out possible conflicts with the requirements of the Social Security Act and the Federal Unemployment Tax Act and to raise questions concerning the desirability of the proposals. Thus, future issues of conformity with the federal laws often can be avoided, and suggestions can be offered for improvements in the substance or legal phraseology of the amendments. Most state agencies are glad to avail themselves of this service and welcome advice on legislation, but a few have shown a tendency to resent suggestions and to seek advice only on questions of legal conformity. More and more the federal role is becoming that of advising and cautioning states on their own proposals rather than of developing and suggesting amendments to perfect the unemployment compensation system.

#### CONFORMITY TO FEDERAL LAWS

The Social Security Act and the Federal Unemployment Tax Act contain three sets of requirements with which a state unemployment compensation law must conform to qualify the state for grants and to make

effective the 90 per cent offset against the federal tax. In each case the Social Security Board makes the determination on conformity.

### *Conformity Requirements*

To entitle employers to credit their contributions to the state unemployment compensation fund against the federal unemployment tax, the state law must satisfy the following requirements:<sup>11</sup>

(1) All compensation must be paid through public employment offices or such other agencies as the Social Security Board may approve.

(2) No compensation may be payable for unemployment occurring within two years after contributions begin to accrue.

(3) Receipts of the state unemployment compensation fund must immediately be paid into the unemployment trust fund in the federal treasury.

(4) Money withdrawn from the unemployment trust fund must be used only for the payment of unemployment compensation, exclusive of administrative expenses.<sup>12</sup>

(5) Compensation must not be denied because of refusal of work "if the position offered is vacant due to a strike, lockout, or other labor dispute; if the wages, hours, or other conditions of the work offered are substantially less favorable to the individual than those prevailing for similar work in the locality;" or if employment is conditional upon joining a company union or resigning from or refraining from joining a bona fide labor organization.

(6) All rights, privileges, or immunities conferred by the state law must be subject to the power of the legislature to amend or repeal it.

The first of these conditions was intended to discourage the use of agencies other than public employment offices in the payment of benefits. In at least two states the Social Security Board has used the authority conferred by this provision to prevent the payment of unemployment compensation through local relief offices. The second requirement was designed to permit the accumulation of a reserve balance before benefits became payable. The third and fourth safeguard unemployment compensation reserves by compelling the states to keep them in the federal unemployment trust fund for investment by the Treasury Department. The fifth helps to protect labor standards by preventing denial of bene-

<sup>11</sup> Section 1603 of the Federal Unemployment Tax Act. 53 Stat. L. 1391.

<sup>12</sup> This and the preceding requirement are subject to an exception for refunds of sums erroneously paid into the state unemployment compensation fund.

fits for failure to accept employment that might be disadvantageous to workers. The final requirement preserves the freedom of the state to alter or abolish its unemployment compensation system. Shortly before the due date of the federal unemployment tax, the Social Security Board each year must certify to the Secretary of the Treasury the state laws it has approved under these provisions, excluding any which, after opportunity for a hearing, it has found to be no longer in conformity with the terms of the federal act.

The second set of federal requirements relates to eligibility for grants for the administrative expenses of state agencies.<sup>13</sup> It includes the first, third, and fourth items listed above and the provisions of section 303(a) relating to administration which were quoted on page 14. In addition, it stipulates that states shall afford all persons, whose claims for benefits have been denied, an opportunity for "a fair hearing before an impartial tribunal" and shall supply information on recipients of unemployment compensation to federal public works and work relief agencies upon request. A certification of conformity with these requirements must accompany each grant authorized by the Board.

The third set of conditions affects only states where employers' contribution rates are being reduced by the operation of experience rating, employer reserve account systems, or guaranteed employment plans.<sup>14</sup> To enable employers whose rates are so reduced to obtain credit toward their federal tax equivalent to 2.7 per cent of their payrolls (that is, the full 90 per cent offset against the 3 per cent federal levy on payrolls), the state provisions governing rate reductions must conform to certain federal standards. For employer reserve account systems and guaranteed employment plans, definite requirements are imposed as to the size of reserve necessary to qualify for reductions. For experience rating, however, the only condition set up by federal law is that no employer's rate shall be lowered except on the basis of three years' experience directly relating to the unemployment risk. Compliance with these requirements is certified annually by the Social Security Board before the federal unemployment tax becomes due.

### *Determination of Conformity*

For purposes of conformity under the federal acts, the term "law" embraces much more than the state unemployment compensation statute.

<sup>13</sup> Section 303(a) of the Social Security Act. 49 *Stat. L.* 626.

<sup>14</sup> Section 1602 of the Federal Unemployment Tax Act. 53 *Stat. L.* 1388.

It also includes other state legislation affecting the administration of the unemployment compensation system and court decisions and the opinions of attorneys general interpreting or amplifying these statutes, together with the rules, regulations, and general interpretations issued by the agency. In some cases, such as the hearing of benefit appeals, even a procedure may involve questions of conformity. Decisions on benefit appeals are also scrutinized somewhat and occasional conformity questions raised. As the Board must periodically certify its findings on conformity, it requires states to submit copies of all such materials and maintains a continuous review of their conformity to the federal provisions. The responsibility for this review is divided between the Bureau of Employment Security and the General Counsel of the Federal Security Agency, who has a staff of attorneys specializing in unemployment compensation. The former examines regulations and procedures from the standpoint both of administrative soundness and of conformity with the federal acts and notes lack of compliance in actual operation, while the latter reviews state materials from the strictly legal standpoint and advises the Board thereon.<sup>15</sup>

As most of the requirements of the federal acts are rather clear and specific, they have raised few complex problems of interpretation for the Board. The vaguest and broadest provisions are those of section 303(a) of the Social Security Act that state laws must provide for such methods of administration as the Board finds reasonably calculated to insure full payment of benefits when due, and must afford an opportunity for a fair hearing before an impartial tribunal if benefits are denied. When state laws were originally being reviewed for approval, a list of essentials was prepared, most of which related to these two parts of the Social Security Act. By far the greater number of these items had to do with fair hearing. Among them were such basic requirements as that claimants be given prompt notice of benefit decisions and the reasons therefor, that a reasonable time be permitted for taking appeals, that the appeals procedure must not be so burdensome as to discourage appeals or necessitate

<sup>15</sup> To illustrate the way in which a regulation or administrative practice may raise questions of conformity: Indiana adopted a rule that a worker's earnings would not be counted in computing his benefits unless his employer had paid the contribution due on them. The employer's tax delinquency, therefore, caused a denial of benefits. The General Counsel raised the question whether this did not constitute a failure to pay benefits when due. Another state, whose law at the time did not fix a definite minimum amount of earnings to qualify for benefits, arbitrarily adopted the practice of ignoring claims of persons whose base period earnings were less than \$75. This was not warranted by its law and constituted a denial of benefits when due.

the employment of counsel, that claimants have the right to produce evidence and present testimony, and that the composition of the appeals tribunal be such as to assure impartiality. The items on methods of administration dealt mainly with powers essential to enable the state agency effectively to administer the law. Among them were authority to require employers to keep the records and file the reports necessary for determining liability under the state act, and the power to institute court proceedings for the collection of delinquent contributions. Since the initial period a considerable body of interpretations and declarations of Board policy has developed around both of these provisions of the Social Security Act.

Other principal points upon which the Board has insisted in passing upon state laws are that eligibility for benefits must be contingent upon the claimant's loss of work and not merely upon his loss of earnings, and that benefits must not be payable when the claimant's physical or mental disability would prevent acceptance of employment that otherwise would be suitable. This distinction between unemployment and disability benefits has been derived more from the fundamental nature and purpose of unemployment compensation than from any single provision of the Social Security Act.

It is significant that the Social Security Board has never refused to approve a state law formally submitted to it.<sup>16</sup> Large numbers of conformity questions have been raised by the staff, and states have often been warned; but either the difficulty has later been removed by amendment or other state action, or it has eventually been passed over by the Board. Frequently, defects in legislation have been rectified by opinions of the attorney general of the state or by regulations of the agency. For example, many of the detailed requirements on fair hearing are covered by state regulations and procedures rather than by legislation. Nevertheless, a strict application of the tests of conformity used by the General Counsel's Office and the standards announced by the Board undoubtedly would disqualify many states for grants. When the issue has been squarely presented to it, the Board has usually chosen to accept for the time being state provisions of doubtful conformity and to press for remedial action rather than to risk withholding grants and the probable

<sup>16</sup> The original Utah law was clearly not in conformity with the provisions of the Social Security Act and was not formally submitted to the Board. This law was repealed and a substitute measure enacted and submitted.

suspension of state operations. Grants, however, have often been delayed pending the adoption of corrective measures essential to conformity.

Because the Social Security Act conferred no specific authority for the issuance of federal regulations and standards, the conformity provisions have been stretched by interpretation to cover problems which might more appropriately have been treated by regulation, if indeed they should be made the subject of definite federal requirements at all. Furthermore, there has been a tendency for the federal staff to confuse examination of state actions for soundness with review for conformity to federal law. There has been a temptation to try to find conformity issues in situations where the real question has been one of policy rather than of law. In short, legal conformity has at times been used as a bogey to frighten states into accepting federal views when the matter at issue actually has been a subject of state discretion, and advice and persuasion should have been used. Naturally, this practice has come to be recognized and resented by the states. Its dangers have led to efforts by the Board to curb its use in dealing with state problems.

Inasmuch as a finding of nonconformity automatically shuts off grants, it is much too drastic a measure for ordinary cases. Most of the points on which conformity questions have arisen have not been sufficiently vital to warrant withdrawal of support, and the question has either been dismissed by the Board or left to be worked out by subsequent negotiation. Yet even though the issue is ignored or deferred by the Board, it may cause embarrassment and hardship by delaying grants. Under the procedure followed for several years, conformity questions usually came to a head at budget time, and the necessary negotiations inevitably tended to hold up grants. To reduce delay, the Board has provided that such questions shall be taken up with the states upon discovery and threshed out before the budget period if possible; but even so, they tend to pile up at that time. The severity of the penalty and the danger of interfering with the orderly operation of state agencies would seem to indicate that conformity issues should be raised only after thorough investigation of the circumstances, and then only where the defect in the state law or practice is sufficiently material to have serious effects on the program.

## CHAPTER IV

### THE 100 PER CENT GRANT FOR ADMINISTRATION

EXCEPT FOR ABOUT \$3,000,000 of state and local funds for employment service, the entire annual cost of administering the employment security program is financed from federal grants made by the Social Security Board under the Social Security and Wagner-Peyser Acts. From British experience, the President's Committee on Economic Security estimated that administrative expenses of unemployment compensation, including the greater part of the cost of the employment service, would amount to approximately 10 per cent of the contributions collected for the insurance system. This estimate accounts for the 90 per cent limit on the offset allowed against the federal unemployment tax. The 10 per cent of this tax which is actually collected by the federal government was intended to provide the revenue needed for administrative grants, though it was not legally set aside for that purpose. The proceeds of the unemployment tax are treated as general federal revenue, and an annual appropriation is made by Congress for grants for the administration of unemployment compensation. Actually, the federal tax now yields somewhat more than the amount of the grants. The Social Security Act fixes a limit of \$80,000,000 on the appropriation, but the tax produced about \$106,100,000 for the federal treasury in the year ending June 30, 1940.<sup>1</sup>

Within the appropriation made by Congress, the Board has wide discretion in the determination of grants for employment security agencies under the Social Security Act. The Act merely provides that the Board shall award such amounts as it finds "to be necessary for the proper and efficient administration" of the state unemployment compensation law, "based on (1) the population of the state; (2) an estimate of the number of persons covered by the state law and of the cost of proper and efficient administration of such law; and (3) such other factors as the Board finds relevant."<sup>2</sup>

As yet the Board has been unable to devise a definite formula for the

<sup>1</sup> The Social Security Act originally set a limit of \$49,000,000 on appropriations for unemployment compensation grants. This sum was definitely inadequate and was raised to \$80,000,000 by amendment in 1939. Actual administrative expenditures of state agencies in the fiscal year 1939-40 amounted to \$65,551,505.

<sup>2</sup> Section 302. The words "and efficient" were inserted in 1939.



determination of grants, and in all likelihood it never will be able to construct one. Its problem in arriving at the necessary cost of "proper and efficient administration" of a state agency is very similar to that of a legislative body in fixing the appropriation of a given bureau. It must consider the resources available for expenditure, the nature, magnitude, and worth of the program of the particular agency in relation to the activities of other agencies, the past level of expenditures, and any special conditions affecting administration and costs. In short, the task of the Board is largely one of budget analysis. Formulas and cost standards may be developed which will be helpful in appraising the needs of different states, but no substitute can be found for thorough review of detailed budgets, supported by an examination of operating programs. Population and the number of covered workers provide no adequate measure of administrative costs.

The Board early decided that it must base its grants on itemized state budgets, and prescribed forms and regulations governing their content and the procedure for their submission and review.<sup>3</sup> The budget as revised and approved by the Board becomes in effect the appropriation for the state agency. Not only does it establish the total amount of the grant, but it also fixes the sum which may be expended within each budget category. Grants are paid to the states in quarterly installments, and the unexpended balance at the end of one budgetary period is deducted from the approved budget for the next in determining the succeeding grant.

A different set of principles governs the action of the Board in making grants for employment service under the Wagner-Peyser Act. In this case, the federal appropriation is apportioned among the states according to population, and grants must be matched by state and local funds. Inasmuch as the Act limits this appropriation to \$3,000,000 a year—only a small fraction of the cost of maintaining the employment office system—the Social Security Board merely credits the Wagner-Peyser grant and the state matching funds against the total approved budget for unemployment compensation and employment service, and the remainder is financed by grants under the Social Security Act. Wagner-Peyser grants

<sup>3</sup> Social Security Board, *Instructions to State Unemployment Compensation Agencies Relative to Fiscal Affairs in Connection with Grants Made Pursuant to Title III of the Social Security Act*, Instruction UC-501, December 1936. These instructions have been revised several times and considerably elaborated. The current provisions are contained in *Instructions to State Agencies Relative to Fiscal Affairs in Connection with Grants Made for Expenses of Unemployment Compensation and Employment Service Administration*, Instruction ES-501, September 1939.

are paid quarterly in advance, subject to later adjustments if the state does not spend an equal amount of its own money.<sup>4</sup> Eligibility for these grants is contingent upon federal approval of the plan of operation of the state employment service and upon compliance with federal standards and regulations relating to employment service. To qualify for a social security grant, the state must match its current Wagner-Peyser apportionment in full.

#### EFFECTS OF THE 100 PER CENT GRANT

The wisdom of the unmatched grant by the Social Security Board for unemployment compensation administration has often been questioned. It involves a radical departure from the established grant-in-aid practice of the federal government and has created many new and difficult problems for both the federal and the state agencies concerned. As a unique experiment in federal-state relations and because of its important effects on the administration of the employment security program, the 100 per cent grant for unemployment compensation administration deserves careful examination.

The 100 per cent grant doubtlessly accelerated the establishment of a nation-wide system of unemployment compensation. Coupled with the offset against the federal tax, it left the states no excuse for failing to enact unemployment compensation laws. Delay meant the loss of large amounts of revenue that might be applied to unemployment benefits, while action did not impose an added drain on existing state resources.

#### *Adequate Financing of State Administration*

As a continuing arrangement the 100 per cent grant assures reasonably adequate financing of unemployment compensation administration in all states. It is possible, of course, that Congress may fail to make sufficient appropriations for the grants; but this danger is small by comparison with the virtual certainty that some states would refuse, or lack the resources, to provide adequate funds for matching federal grants made in the usual manner. Even if half the proceeds of the federal unemployment tax were returned to the states to enable them to match the federal grants, a number of states would have to draw on other revenues to obtain the sums required to operate the system.

<sup>4</sup> Under the rules of the Social Security Board, expenditures for employment service are to be charged first to state and Wagner-Peyser moneys in equal amounts and the excess to the grant under the Social Security Act.

The 100 per cent grant serves to equalize the burden of financing unemployment compensation administration. This is a matter of importance, for experience already demonstrates that administrative costs vary widely among the states. For example, the large, densely populated industrial states have low unit costs, and the sparsely settled states with small numbers of insured workers have high unit costs. Administrative expenses range from less than 6 per cent of contributions in some big industrial states to more than 15 per cent in a few thinly populated states. Inasmuch as unemployment is a problem of the economic system and unemployment compensation is a national program, it is only fair that the cost of administration should be equalized to a large degree.

### *Tendency toward Extravagance*

While complete federal financing has evened the burden and provided the necessary funds for launching the unemployment compensation program in all the states, there can be no question that it also has lessened state interest in the economical administration of the system. As the state government bears none of the cost, it has little direct incentive to strive for economy. In fact, it has an inducement to spend freely, as it makes the appointments and the expenditures. State administration of unemployment compensation is a case of power to spend without responsibility for raising the funds expended. The early budgets submitted by unemployment compensation agencies gave ample evidence of this fact. It was not surprising that some agencies should try to obtain unnecessary equipment and unduly elaborate quarters and furnishings, or that some states should seek to inflate the personnel and raise salary levels for patronage purposes.

Yet most of the waste found in unemployment compensation budgets has been due to lack of experience rather than to extravagance. Until benefits had been paid for a time, state officials simply did not know how much personnel and equipment would be required or what types of employees and machinery might be best adapted to the undertaking. Under the circumstances, it was natural for administrators to over-estimate their requirements in order to be on the safe side. Against the cases of attempted extravagance that might be cited must be aligned others in which state salary scales and furniture requests were more modest than the federal agency itself would probably have proposed under the circumstances. Much more has depended upon the temperament of the individual official and the tradition of the state administra-

tion than upon the method of financing the agency. Nevertheless, it is fair to say that budget requests would almost certainly have been considerably more conservative if the states had been providing a large part of the money.

### *Relaxation of State Controls*

It is also true that the lack of a direct financial stake in the administration of unemployment compensation has resulted in the relaxation—amounting in some cases to partial discontinuance—of normal state administrative controls over employment security agencies. For example, one can literally count on the fingers of one hand the states in which the state budget officer actually reviews and revises the budgets of the employment security agency.<sup>5</sup> In most states he does not even see them. If they are presented to him, it is merely to obtain his signature before submission to the Social Security Board. Unemployment compensation administration is not included in the state budget or the appropriation act, and its requirements are not ordinarily examined by the legislature.

As a rule, state fiscal officers make little effort to control the expenditures of the employment security agency, except to see that they do not exceed the available funds and that they conform to the customary expenditure regulations of the state, such as those on automobile mileage allowances, reimbursement of travel expenses, etc. Vouchers pass through the regular channels and receive the usual scrutiny by fiscal officers, but many states do not make as complete a post-audit of the finances of the employment security agency as of other departments. Some states with centralized purchasing have also allowed employment security agencies unusual latitude in making their own purchases. The relaxation of state controls is due in a measure to lack of interest in the economical administration of employment security agencies and in part to a belief that such controls would largely duplicate those maintained by the Social Security Board.

### *Increased Federal Supervision and Control*

Complete federal financing and the inadequacy of state control over the expenditures of employment security agencies have greatly enlarged the responsibilities and complicated the task of the Social Security Board.

<sup>5</sup> The outstanding exception is New York, where the state budget officer makes a thorough review of the employment security budget and himself presents it to the Social Security Board.

To an unusual extent Congress and the public have viewed the Board as accountable for the character of unemployment compensation administration in the states. This has increased the watchfulness of the Board and spurred its efforts to raise the level of efficiency of state agencies. It is significant that no other federal agency exercises as close supervision over the administration of federally aided state activities as does the Social Security Board in the field of unemployment compensation.<sup>6</sup> And the Board wields a much greater influence in this field than in that of old-age assistance, where it furnishes only half the funds.

While the 100 per cent grant has increased the need for federal supervision, it has also facilitated the establishment of federal controls and standards of administration. The failure of the Social Security Act to provide specifically for national standards and regulations has more than been offset by the discretion vested in the Board as to the determination of grants. The power to fix the total budgets of state agencies practically compels the Board to develop its own tests of need and national standards of proper and efficient administration. In reviewing and revising these budgets, it cannot but delve into the validity and effectiveness of the methods of operation and make decisions vitally affecting the administration of the agencies.

Despite talk of states' rights and the contention that in making grants the federal government is merely returning to the states a part of the payroll tax revenue which it has withheld from them, state officials rather generally recognize that complete federal financing of administrative costs creates a different federal-state relationship entitling the federal government to a greater voice in the conduct of the enterprise. It is admitted, perhaps grudgingly, that so long as the states are dependent upon the national government for the money, they must expect it to exercise considerable supervision. In fact, at least one governor is reported to have said that he looked upon unemployment compensation as a federal, rather than a state, program. The method of financing employment security agencies and the high degree of federal supervision which it has entailed have undoubtedly set them apart from other state departments and tended to give them a quasi-federal status.

<sup>6</sup> The nearest approach was the United States Employment Service in the administration of grants under the Wagner-Peyser Act. This law confers unusually broad authority to set standards, and the United States Employment Service availed itself of the opportunity to increase the efficiency of state administration. To a considerable degree it pioneered the way for the Social Security Board. The methods used by the United States Employment Service are described in Atkinson, Odencrantz, and Deming, *op. cit.*, Chapters 4 and 10.

In one important respect, however, the fact that the federal grant is unmatched reduces the effectiveness of federal supervision: it greatly increases the difficulty of recovering the funds in case of improper expenditure. If the state is required to bear a fixed proportion of the cost, expenditure items disallowed by the federal auditors can be charged to the state's appropriation and be deducted from the matching amount in fixing the next apportionment. Thus, the federal government can prevent misuse of its grants and penalize the state which fails to observe the conditions attached to them. But with the 100 per cent grant, there is no state appropriation that can be charged. Any reduction of the next allotment below the amount of the approved budget of the state agency may restrict its operations and impair the program for which the grant is made. This deprives the federal government of a useful sanction for the enforcement of minimum standards of administration and compels it either to dismiss the violation of its requirements with an admonition or to consider the complete withdrawal of federal aid. The latter is such a powerful weapon that it can rarely be employed. The threat of use is harmful to state relations, and actual use is disruptive of the program. The lack of a more practicable sanction to enforce compliance with essential federal regulations is one of the serious defects of the present method of financing unemployment compensation administration.<sup>7</sup>

#### ALTERNATIVES TO THE 100 PER CENT GRANT

Because of the problems created by the existing type of grant, various alternative methods of financing unemployment compensation administration have been proposed. Some of the principal possibilities will be examined.

##### *Complete State Financing*

One suggestion offered by some state officials is that the federal government simply return to each state the amount of tax collected in it. Another having the same effect is to raise the offset against the federal tax from 90 to 100 per cent and permit the states to make a corresponding increase in contribution rates, from which they would then meet their own administrative expenses. Either of these schemes would auto-

<sup>7</sup> As indicated in Chapter VI, the federal agency would be in a better position to obtain compliance with its regulations if the 100 per cent grant were made as a reimbursement rather than as an advance.

matically turn the money over to the states. This would eliminate federal review of state budgets and with it most of the federal supervision. Without some discretion in the determination of grants, the Social Security Board could not obtain acceptance of national standards and would have only an advisory relation to state agencies.

Such a change would practically convert the federal-state system of unemployment compensation into a collection of substantially independent state systems. The result would be a marked reduction in administrative efficiency. Many states which have accepted the merit system only under federal pressure would soon revert to spoils politics in the selection and removal of personnel. Wholesome regulations on purchasing and fiscal administration—often adopted to meet federal requirements—would probably be abandoned in many cases. The influence of the Social Security Board for uniformity and coordination among agencies would be undermined. Some of the smaller states, where administrative expenses inevitably exceed 10 per cent of contributions, would find it impossible to maintain their agencies from the revenue which this kind of an arrangement would supply.

If the federal unemployment tax were left on the statute books subject to a 100 per cent offset provision, some kind of state unemployment compensation system would still be necessary to enable employers to claim the credit against the federal tax, though it might be a seriously defective system. But, if the federal tax were repealed to make room for an increase in state contribution rates, there would be nothing to prevent states from abolishing unemployment compensation entirely. In view of the newness of the program, it is not unlikely that a number of states would do so. For those who sincerely wish to see unemployment compensation preserved and made more effective, these substitutes for the present method of financing are far too dangerous to deserve serious consideration.

### *Matching Grants for Cost of Proper Administration*

An alternative which merits more careful examination is a matching grant somewhat similar to that now made by the Social Security Board for the administration of aid to the blind. This grant amounts to one-half of the administrative expenses "found necessary by the Board for the proper and efficient administration of the state plan" of assistance to the blind.<sup>8</sup> This provision enables the Board to review state budgets and

<sup>8</sup> 53 Stat. L. 1397.

fix the total to which it will contribute on an equal matching basis, but does not prevent the state from spending a greater sum, provided it is willing to meet the excess entirely from its own funds.

If applied to unemployment compensation, this plan would require raising the offset against the federal tax from 90 to 95 per cent to enable the states to obtain the additional revenue needed for matching federal apportionments. To give the states a real incentive for economy in the administration of unemployment compensation, the 5 per cent addition to their payroll levies would have to be treated as general state revenue available for any purpose, just as the proceeds of the federal unemployment tax are now treated by the federal Act. Economy in unemployment compensation administration would then increase the funds available for other state uses and would help to balance the state budget. If the new revenue were restricted to unemployment compensation purposes, state officials and legislatures would probably show little, if any, more concern about economy than they do under the present arrangement, as it would neither release money for other activities nor reduce the taxes they must levy.

Special provision would need to be made for the less populous states which cannot be expected to administer unemployment compensation on an amount no greater than 10 per cent of contributions. This could be done by permitting the Social Security Board to make a supplementary grant equal to the sum by which the necessary cost of proper and efficient administration in any state exceeded 10 per cent of the payroll tax. Because of the small size of the states affected, these supplementary grants would not add greatly to the federal appropriation required. With a 95 per cent offset against the federal payroll tax, the 5 per cent collected by the federal government would more than cover the regular matching grants and supplementary grants, because the total cost of proper administration falls much below the 10 per cent level in large industrial states.

This method of financing would have several advantages over the present plan. By requiring the state to bear a substantial part of the cost, it would provide a genuine incentive for economy and the application of the usual state administrative controls. It would also enable the Social Security Board to deduct from its grants and the state matching funds any expenditures made in violation of federal standards. This would provide a means of safeguarding federal grants and penalizing infractions which now can be dealt with only by threat of complete withdrawal of federal support. The combination of these things would allow the Board



to discontinue the itemization of grants and the advance approval of various transactions. As the Board would still have to determine the necessary cost of proper and efficient administration, it would continue to review detailed budgets, though its revisions need only affect the total amounts granted. It would also have the same authority as it now possesses to establish minimum standards of administration as a condition of eligibility for grants. Thus, the Board would retain the means of preventing waste and of improving state administrative practices while being relieved of the necessity of maintaining many of the minute controls which have greatly complicated its work and tended to impede state operation. On their side, the states would gain a real responsibility for the conduct of unemployment compensation and greater flexibility in the administration of their agencies.

The principal objection to such a plan is that some states might divert to other uses too much of the additional revenue obtained from contributions and fail to make sufficient appropriations for the administration of unemployment compensation. This is a possibility, but it is a risk that all other state activities must run. Either this risk must be assumed or the attempt to create an incentive for economical state administration must be abandoned. If the main concern is to assure adequate support in all states, the 100 per cent grant is the best plan. If it is deemed desirable to stimulate state interest in the cost of administration, then the state must participate in the financing on a basis which makes the reduction of costs advantageous to it. There appears to be no method of penalizing extravagance and rewarding efficiency which does not entail the possibility of niggardliness.<sup>9</sup>

### CONCLUSIONS

It is evident that the 100 per cent grant imposes a much heavier responsibility upon the federal agency than does the usual type of matching grant, and that it compels greater watchfulness and closer supervision to avoid extravagance. Yet, experience with unemployment com-

<sup>9</sup> It has sometimes been suggested that the additional revenue released to states by a 95 per cent offset should be available only for unemployment compensation purposes and that the amounts not used for administration should go into the reserve fund. While some agencies would strive to keep down costs in order to build up their reserve funds, others would make little effort to do so. Moreover, this arrangement would not stimulate the interest of state fiscal officers and the legislature in the cost of unemployment compensation administration, as the level of unemployment compensation expenditures would not affect the rest of the state budget.

pensation thus far indicates that unmatched grants can be administered successfully and without serious waste. Most state unemployment compensation administrators have sincerely desired to make a good record and have striven to keep costs within reasonable limits. Moreover, the lessened interest of the state government in economical operation has been counterbalanced by intensified federal efforts for efficiency.

As the 100 per cent grant has been administered by the Social Security Board, it certainly has not produced the unfortunate results that might have been feared, but rather has been used as a powerful instrument for improving administrative methods in many states. On the basis of extensive field studies the author is inclined to believe that, in general, employment security agencies are being administered quite as efficiently as other state departments having equally difficult problems. In fact, he would not be surprised if a careful comparison would indicate a higher level of efficiency, though exceptions would have to be made for certain states. Any appraisal must, of course, take into account the newness of the program. Some waste was inevitable in launching an undertaking as intricate as unemployment compensation. The initial costs were bound to be high, but they have already been sharply reduced.

In so far as personnel, procurement, and certain fiscal practices are concerned, employment security agencies compare very favorably with other state departments, and in many states are definitely superior. While the character of these practices does not constitute a true measure of the overall efficiency of an agency, it has such far-reaching effects upon the level of administration as to give it considerable significance as an index.

Nevertheless, if the federal-state system is to be the permanent plan for administering unemployment compensation, serious consideration might well be given the desirability of substituting for the present method of financing a type of matched grant somewhat on the order of that described above. To assign broad administrative authority to states without requiring them to bear a substantial part of the cost is anomalous and, in spite of federal efforts, potentially dangerous. The finances of state employment security agencies should be subjected to the same scrutiny by state budget officers, auditors, and legislatures as those of other administrative units. The absence of interest and control is unhealthy and imposes an excessive burden on the Social Security Board. Greater state financial responsibility and a broader type of federal supervision would seem more appropriate to an enterprise actually carried on by state agen-

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cies. It ought to be possible to devise a form of matched grant which would increase state interest and responsibility, yet retain in the federal agency adequate authority to review budgets and operating programs and to maintain sound minimum standards of administration.

## CHAPTER V

### BUDGET AND GRANT PROCEDURE

THE BUDGETS which the Social Security Board requires of state employment security agencies present expenditure estimates in about the same degree of detail as a modern municipal budget. Estimates are divided into fifteen categories by types of commodities and services in accordance with the expenditure classification of the federal government, and the request for each category must be supported by appropriate explanations and schedules. Personal services are shown by organization units and broken down by classes of positions and salary rates, with a segregation of permanent and temporary positions. Equipment estimates are itemized in detail. Formerly, separate budgets were required for unemployment compensation and employment service, but now one budget is submitted covering both functions.<sup>1</sup>

The quarter was originally adopted as the budget period. During the first few years, the agencies were undergoing such rapid development that it was impossible to foresee their needs for more than three months. In fact, even quarterly estimates involved a large element of guesswork because of the number of unknowns in the program. Quarterly budgeting, however, imposed a heavy burden of fiscal work on both state and federal agencies. One set of estimates had scarcely been approved by the Board and the necessary adjustments made in the states before it was time to start the preparation of another. The regional staff of the Board was constantly engrossed in budget problems and had little time to devote to other matters. State officials also had to spend an extraordinary proportion of their time on fiscal problems, while the agencies had to live a hand-to-mouth existence. Though this was unavoidable in the beginning, the desirability of a longer budget period was generally recognized. After the first year of benefit operations the Board permitted states with at least six months of benefit experience to go on a semi-annual budget basis. By 1940 nearly all the states were operating on this basis.

An annual budget period will be feasible after there is somewhat more

<sup>1</sup> Joint use of personnel and facilities made an accurate division of estimates between unemployment compensation and employment service impractical because the budget of each usually included part of the cost of the other function.

experience on which to base estimates. The longer period would reduce the time consumed in fiscal work and permit more stable operation. In the past, agencies have often had to make hasty adjustments in personnel and programs because of unexpected changes in their quarterly grants. In a measure, annual budgeting would simplify the preparation of estimates because over a year the fluctuations in work load would tend to cancel out, but it would also greatly increase the difficulty of forecasting the total volume of benefit claims to be handled. Any system of annual budgets and grants, therefore, must provide for reserves or supplementary grants to meet unforeseen changes in the labor market. In addition, it should require state agencies to allot their funds by months or quarters for better fiscal planning and control of expenditures.

The preparation of the budget is normally a responsibility of the business manager or fiscal officer of the state agency, under the direction of the head of the agency. As a rule, the director himself takes rather an active part in the formulation of the budget. Many agencies call upon the heads of the principal units for estimates of their needs, but this is by no means universal practice. If the agency is a part of the state labor department, the budget is usually referred to the commissioner of labor for approval before submission to the Social Security Board.

### BUDGET REVIEW

The federal review of state budgets was originally handled by a small group of analysts in the central office of the Bureau of Unemployment Compensation. State administrators generally came to Washington to discuss their estimates directly with the federal officials. The uncertainties of the enterprise and the lack of any measures of expenditure requirements made the review, like the preparation, of the estimates rather a blind and difficult task. In some cases large reductions were made because requests clearly exceeded needs and the ability of the agency to build up its organization. To cite an extreme example: one populous state submitted an initial budget for over \$250,000, which was cut to about \$80,000 by the Bureau of Unemployment Compensation, but actually less than \$50,000 was spent during the quarter.

In general, the Bureau sought to forestall obviously extravagant and unnecessary proposals, and to compel careful preparation and reasonable substantiation of state requests. Elaborate quarters and furnishings were frowned upon, and a special effort was made to keep salaries in

agreement with those for similar positions in the state government. The application of these policies often led to numerous detailed adjustments in salary rates and equipment estimates. Many of these changes were small—a \$5-a-month cut in the salary for a particular position—and some a bit petty, for instance, the deletion or reduction of an item for desk sets or a change in the number or price of office chairs.<sup>2</sup> Yet they may have made state officials somewhat more conservative in the preparation of subsequent budgets. To a large degree, budget review amounted in the early stages to little more than a rough application of common sense with a certain amount of higgling or trading to keep expenditures down.

### *Regional Review*

In the second year of the program, the Bureau began sending its budget analysts into the states to make a preliminary review of estimates and to go over the requests with officials of the agencies. The regional representatives regularly stationed in the field participated in these conferences. The field review was followed by further revision by the Bureau in Washington before the budget was submitted to the Board. Subsequently, most of the budget analysts were transferred to the field as assistant regional representatives, but the central review was retained.

The regional representative has gradually come to play a major role in the budget process. While he is not supposed to participate in the preparation of state budgets, he occasionally has done so, and he often exercises a considerable influence on their preparation. State officials commonly consult him before or while formulating their estimates to obtain his advice on problems and to ascertain the probable reaction of the Washington office to their proposals. Also, the budgets often reflect his efforts to induce agencies to effect changes in line with the recommendations of the federal Bureau. In a few cases the regional representative is so close to the agency and so thoroughly acquainted with its operations that he functions almost as one of its officials and takes part in most of the important administrative discussions. On the other hand, some agencies maintain rather an arm's-length policy in their dealings with the regional staff and consult it only when necessary to avoid future complications. Ordinarily, relations are on a friendly and informal basis which permits the regional representative to exert a substantial influence without raising questions of prerogative. Much, of course, depends on

<sup>2</sup> In one case an item of \$13.80 for two desk lamps was cut to \$4 because \$2 lamps were considered adequate. Such adjustments were not uncommon.

the ability and personality of the representative and the attitude of the state officials.

The budget is due at the regional office two months before the beginning of the fiscal period. After making a careful analysis, the regional representative or one of his assistants visits the state and goes over the estimates in detail with the officials of the agency. Proposed changes are usually discussed and many are agreed upon at this time. The regional representative then completes his revision and transmits the revised budget to the Bureau with explanations and recommendations. New questions of policy and particularly difficult issues that might adversely affect his relations with the state are commonly referred to the central office for decision.

### *Central Review*

Upon receipt at the Bureau of Employment Security in Washington, the budget is checked for mathematical accuracy and subjected to an elaborate routine examination. Estimates are compared with previous expenditures for consistency; personal service items are examined for adherence to the approved classification of positions and the salary schedule and for the discovery of abnormal salary increases; rental items are compared with the terms of the leases; and equipment requests are checked against price lists and the agency's inventory to verify prices and prevent unnecessary purchases.

The results of this routine examination, together with the copy of the budget bearing the regional representative's revisions, go to the section of the Field Division which handles relations with the particular state.<sup>3</sup> Here the budget is reviewed for the validity and reasonableness of the requests, with particular emphasis upon staffing, quarters, and equipment and upon the desirability of proposed changes in organization and procedure. The review of the budget brings to a head many issues arising out of field studies and the analysis of materials received from the states.<sup>4</sup> Frequently, it opens up active negotiations for the adoption of federal recommendations and enables the Bureau to apply financial pressure to obtain their acceptance. Since the early months of benefit

<sup>3</sup> As indicated in Chapter II, the work of the Field Division is carried on through four sections, each responsible for three of the twelve regions.

<sup>4</sup> A good example was the revision of the Indiana budget for the six-month period beginning in July 1939. On the basis of a detailed survey of central and local office operations, the budget was reduced from \$821,236 to \$720,363. In this case the greater part of the revision was made in the regional office.

payment, there has also been a vigorous drive to reduce the cost of operation.

The relative proportion of budget revisions made in the regional offices and in Washington has progressively shifted, with the former comprising an increasing part of the total. The majority of changes now originate in the regions. After some complaint from the regional personnel, the Bureau has adopted the policy of clearing with the regional representative all the revisions it has proposed in order to obtain his advice before presentation of the budget to the Board. As a rule, only those changes are now made which are accepted by the regional representative. This procedure has proved necessary to avoid adjustments which do not take adequate account of local conditions or possible effects on federal-state relations.

### *Board Action on Budgets*

The Bureau presents the revised budget to the Board with its recommendations on the grant. Major questions of policy are normally taken up with the Board, as well as any conformity issues. In view of the breadth of the social security program, the Board has given remarkably close scrutiny to the budgets of employment security agencies and often has gone into considerable detail in its analysis and revisions. The trend, however, is toward confining Board action to basic problems of policy and leaving the detailed application of federal policies to the Bureau. In many cases the Board has attached to its grants definite restrictions or conditions to be fulfilled by the state agency. It has frequently specified that none of the money is to be used for certain purposes or that certain changes are to be made in the operation of the agency. In several grants, for example, it has instructed the agency to unify its local organization for employment service and unemployment compensation.

In the summer of 1938 the Board adopted the policy that each agency must progressively scale down its administrative expenses during the coming year so that by July 1939 they would not exceed 10 per cent of contributions. In pursuance of this policy many budgets were approved by the Board with the condition that certain additional economies were to be effected during the period and that further reductions were to be made in preparing the succeeding budget. When this 10 per cent rule was adopted, expenditures exceeded 15 per cent of contributions in several of the states then paying benefits. The rule was an effective opportunistic device for forcing a rapid reduction of administrative expenses,



but was difficult to justify as a measure of budget requirements. It had very unequal effects on different agencies and soon had to be modified to meet the needs of the sparsely populated states which could not operate on such an amount.

### *Improvements in Budget Procedure*

The major weaknesses of the budget review procedure have been delay, lack of cost standards, and limited knowledge of local conditions on the part of the central office staff. Up to the fall of 1939, grants frequently were not made until after the opening of the period to which they related—sometimes as much as several weeks later. This, of course, caused embarrassment for all parties concerned. While quarterly budgeting prevailed, delays were especially serious as they left the agencies little time in which to effect the economies required to meet budget cuts. Several factors were responsible for delay in making grants. Lateness in filing state budgets was a common cause. The minuteness of the federal review at both the regional and central office levels and the number of different units through which budgets passed were important factors. Efforts to clear up conformity issues and to obtain changes in state organization and methods also slowed down the budget process. The delay of grants has practically been eliminated by placing greater reliance on the regional review of budgets and by adopting the policy of threshing out conformity issues between, rather than at, budget review periods.

Budget review could be further simplified and accelerated by assigning the detailed examination and revision of budgets entirely to the regional offices and reducing the duplication of work between the regional and central staffs. At the same time decentralization would place responsibility on the regional representatives who possess an intimate knowledge of the state agencies with which they deal, and would largely remove the danger of budget adjustments being made without an adequate understanding of local conditions. If the work were shifted to the regions, some increase in regional personnel would be required, and certain records now used by the Bureau in the routine checking of estimates would have to be transferred to the regional offices.

Experience in a few states indicates that it might be worth while to include the state budget officer in the budget conference between the regional representative and the officials of the agency. Though the state budget officer does not have the understanding of unemployment com-

compensation and employment service operations which the regional representative possesses, he has a knowledge of state salary scales, price levels, administrative regulations and procedures, etc., which would be very useful in the examination of the budget. In Connecticut, where the state budget officer has normally participated in the budget conferences, the practice seems to have proved helpful to both parties.

If the detailed revision of budgets were assigned to the regional staffs, the central office review could be limited to a general examination of the revised budget to enable the Bureau to assure itself that the work of the regional office had been properly performed and that the policies of the Bureau and the Board had been observed. Many questions would have to be submitted to the central office for advice or the determination of policy. The maintenance of good relations between the regional staff and the state agency would likewise necessitate the referral of some especially important or delicate budget issues to the Bureau for decision. The central office would also need to examine budgets from the standpoint of comparative costs to see that estimates were being kept in reasonable agreement with federal cost standards and with expenditures in similar states. In addition, decentralization would call for increased inspection of regional offices and for more surveys of state operations by the Bureau staff.

State and federal officials have recognized almost from the outset that the whole budget process—in the states, the regional offices, and the Bureau—would be greatly aided by further expenditure analysis and the development of comparative cost data. The present paucity of information has handicapped the states in preparing their estimates and the Bureau in reviewing their requests. A number of rules of thumb have been devised by the Bureau to aid in the examination of budgets; for example, certain rough indices of personnel requirements, such as a given number of employees per 10,000 insured workers and a certain ratio of field auditors and investigators per 1,000 employers subject to the payroll tax. But these rules have had only very limited value in judging the needs of a particular state. To remedy this situation, the Bureau of Employment Security has undertaken a series of cost studies in cooperation with a number of state agencies. It is hoped through these studies to determine the usual unit costs and staffing requirements of the principal activities involved in the operation of unemployment compensation in states of various sizes and with different types of procedures.

## THE ITEMIZED GRANT

Unlike most federal grants-in-aid, those for unemployment compensation administration have not been made in lump amounts, but have required item-by-item observance of the budget as approved by the Social Security Board. In effect, the revised budget is a detailed appropriation act for the state agency. Any expenditure not in conformity with the approved budget is subject to disallowance by the federal auditors. In the beginning, grants were so divided as to show the central office of the agency and each local employment office separately, and were then broken down by fifteen expenditure categories, and within the category for personal services, by classes of positions.<sup>5</sup> Segregation of employment office expenses by individual offices was soon found impracticable and was abandoned for most expenditure categories.

As the Board's regulations stood in 1940, the approved budget was binding upon most state agencies in the following degree of detail: the total allowance for personal services was subdivided by classes of positions, and, while the state was allowed to make transfers among offices, federal approval was required for adjustments involving changes in the salary rate or the number of positions in any class. Other current expenses were set up in thirteen expenditure categories for the agency as a whole, except that the amounts for rent of premises and for repairs and alterations were subdivided by offices. Equipment items were listed in detail, with a tolerance of 10 per cent permitted for variations in prices.

<sup>5</sup> The expenditure categories are as follows:

- Personal services
- Other current expenses:
  - Supplies
  - Communications service:
    - Telephone
    - Telegraph
    - Postage
  - Travel expenses
  - Transportation of things
  - Printing and binding
  - Advertising
  - Heat, light, and water
  - Rents:
    - Premises
    - Equipment
  - Repairs and alterations
  - Miscellaneous
- Equipment

This classification corresponds to that used by the federal government and differs in details from the expenditure classifications of most states.

Transfers among any of these categories, classes, or items required approval by the Bureau of Employment Security, and expenditures in excess of the allowed amount for any subdivision of the grant were subject to disallowance by the Board's auditors.

The itemized grant was instituted by the Social Security Board primarily because of fear that the 100 per cent grant might lead to extravagance and maladministration. In considerable measure it represented a reaction to the somewhat grandiose proposals submitted by a few states early in the program and to some exasperating requests involving excessive salaries or needlessly expensive equipment.<sup>6</sup> In view of the impossibility of compelling the states to meet such expenditures from their own funds, the Board felt it necessary to impose sufficient restrictions upon the use of federal grants to prevent abuse. Because it lacked minimum standards for the control of state administrative practices and was uncertain of its authority to prescribe and enforce such standards, it resorted to itemized grants and minute control of expenditures as the means of protecting administrative funds.

It is fair to say that the itemized grant has tended somewhat to curb extravagance. It has helped to prevent the creation of needless jobs, and it has, no doubt, forestalled the purchase of a few oriental rugs and some costly furniture for executive offices. But most of the items lopped off the budget could probably have been eliminated almost as effectively by making a corresponding reduction in the total grant and explaining the matter to the state, without requiring item-by-item adherence to the approved budget. In the aggregate the Bureau reduced the budgets of state agencies by more than \$22,000,000 for the fiscal years 1938 to 1940. This reduction, however, was due to detailed budget review rather than to the highly itemized form of the grant. The very fact that the states have returned large sums at the end of most fiscal periods—for the same three years expenditures were nearly \$19,000,000 less than the total approved budgets—indicates that deliberate extravagance has not been as prevalent as some have believed. It would seem to show that, despite the thoroughness of the budget review, total grants have generally exceeded needs and that the states have not been especially prone to inflate their expenditures simply because they have had the money.

Though agency officials have generally sought greater flexibility in the

<sup>6</sup> An early example, which was often cited, was that of a state which included a number of \$50 chairs in its budget. The item was cut, and suitable chairs were eventually purchased for \$12.50.

use of administrative funds, some have viewed the itemized grant as a useful shield against political pressure. Undoubtedly it has many times helped a state administrator to resist pressure for political spoils either in appointments or purchases. He could plead that he had no leeway for a certain expenditure within the grant and that the Bureau would not approve a transfer for the purpose suggested. Or, if need be, he could file a transfer request and intimate to the regional representative that its rejection would not be resented.

But, viewed more broadly, the itemized grant has proved cumbersome and unduly restrictive in operation. It has hampered agencies in effecting desirable adjustments of personnel and procedures within the budgetary period. If an administrator has found that three typists and two stenographers would meet the needs better than three stenographers and two typists, or that \$2,000 of additional office equipment would save \$3,000 in clerk hire, he has had either to delay the change until the next quarter or to submit a transfer request for federal approval. As transfer requests have been reviewed in Washington, several weeks and sometimes months have elapsed before final authorization.

The rigidity of the itemized grant and the delays involved in making transfers have been the more serious on account of the lack of experience on which to base estimates and because of the necessity of numerous changes in plans during the budgetary period as the agencies have gained a clearer understanding of their needs. Moreover, the fluctuations in unemployment have caused wide and often unforeseen variations in work load which have many times compelled changes in expenditure plans. During the early stages of benefit payment, agencies often submitted from twenty to fifty transfer requests in a quarter, and in some of the large states the number occasionally exceeded one hundred.<sup>7</sup> The delay originally experienced in handling transfer requests has been greatly reduced by permitting regional representatives to give tentative

<sup>7</sup> The relative insignificance of many of the transfer requests requiring federal approval is illustrated by the following telegram to the head of a state employment service during the period prior to consolidation of the United States Employment Service and the Bureau of Unemployment Compensation when the two bureaus were acting jointly on budgets and transfers for state employment services:

"Re your telegram 20 you are authorized to transfer \$7 from category telephone to rental equipment employment service second quarter budget for rental eight dozen chairs P— employment office. Submit form 114 to Bureau of Unemployment Compensation and United States Employment Service."

This transfer involved two telegrams across the continent, presumably with a clearance between the two federal bureaus before the reply, and the subsequent submission of transfer request forms to both bureaus for joint signature formally authorizing the transaction.

approval of transfers, subject to review and final authorization by the Bureau in Washington. As the action of the regional representative is usually sustained, states now ordinarily proceed without waiting for confirmation by the central office. Yet the itemized grant remains a clumsy device.

#### ADMINISTRATIVE STANDARDS VS. ITEMIZED GRANTS

At the close of 1938, the Board began to modify its policy with respect to the itemization of grants. In issuing personnel standards for state unemployment compensation agencies, it announced that it would discontinue itemization within the personal services category for states whose personnel procedures satisfied these standards. The following August this change was put into effect for twelve states. The Board also undertook the preparation of other administrative standards looking to the application of the same principle to other expenditure categories. Upon the establishment of suitable standards, the Board indicated that it would confine the breakdown of grants to the fifteen expenditure categories for agencies whose administrative practices met its requirements. When fully effectuated, these policies will give the agencies much greater freedom in the use of their funds, particularly as to expenditures for personal services, rent of premises, repairs and alterations, and equipment.

There are two basic policies which may be followed in attempting to safeguard the 100 per cent grant; and the Social Security Board is shifting from one toward the other. The first is to control the administration of state agencies by requiring prior federal approval of the more important administrative actions. The second policy is to promote efficient administration and to require the use of effective administrative methods, but to leave the agencies free to make their own decisions and direct their own operations. The requirement of strict observance of approved budgets forms the cornerstone of the first method of supervision. As the most significant changes of organization, staffing, or procedure must be reflected in the budget, it enables the federal agency to pass upon them at their inception. When the approved budget is made a binding detailed appropriation, as has been the case with unemployment compensation grants, federal budget review amounts almost to a pre-audit control of state expenditures. If the itemization of the grant were carried to an extreme, the hands of the state administrator could be

ted so completely as to necessitate the assignment of a federal representative to authorize action. This would amount virtually to a federal receivership.

While the Board has never carried its control over agencies to this extreme, the degree of itemization applied to unemployment compensation grants has tended in that direction. It has certainly shifted the final decision on many administrative problems from agency officials to the Bureau of Employment Security in Washington. Shall an employment office be established in Smithville? The Bureau can strike the item from the budget; or, if it accepts the proposal, the terms of the lease on the premises must be submitted for its review. Shall the staff of field auditors be increased from ten to twelve? The approval of the Bureau must be obtained through the budget. Shall a new check-writing procedure be adopted involving certain equipment purchases or a change in the number of clerks and machine operators? Again, a budget item or adjustment must be approved by the Bureau. This plan of supervision necessarily involves the federal agency in a maze of detailed operating problems, many of which cannot satisfactorily be resolved by persons unfamiliar with local conditions. At the same time, this system of control slows down action and does not produce the most effective type of state agency.

In the long run, a combination of lump sum grants and regulations requiring sound methods of administration would seem to offer more hope of producing efficient administration of unemployment compensation and employment service than the plan of supervision originally applied. A policy of this kind tends to raise the level of state administration and strengthen the operating agencies rather than to substitute federal for state judgment on individual administrative issues. It leaves the control of operations definitely to the agency officials who are legally responsible for the administration of the employment security program in their states and are much better acquainted with the setting in which it must be carried on than the federal staff can be. In addition, lump sum grants provide the flexibility needed in handling the highly fluctuating claims load, which is the largest factor in the cost of unemployment compensation administration. A lump sum grant, however, does not imply lump estimates. The requirement of detailed budgets is essential to compel careful financial planning and to provide a basis for the intelligent determination of grants. While the Board has not yet instituted lump sum grants, it is moving in that direction and has definitely

shifted its emphasis from the control of individual expenditures to the improvement of administrative methods.

### ACTIVITIES BUDGETS AND LUMP SUM GRANTS

One of the greatest difficulties in the preparation of budgets and the determination of grants has been the inability to make significant analyses and comparisons of different fiscal periods and among states. The classification of expenditures merely by categories based on the types of services or commodities obtained affords no means of relating expenditures to the volume of work performed by state agencies and of obtaining unit costs. Comparisons by expenditure categories have little meaning, not only because of differences in the work load, but also because of the diverse systems of procedure and plans of organization used in the various states. As the accounts of the agencies have been constructed, however, expenditures can be broken down only in that manner.

#### *Need for Analysis by Activities*

The need of a more satisfactory basis for the analysis of state budgets has led the Bureau of Employment Security to study the possibility of budgeting by activities rather than by objects of expenditure. The administration of unemployment compensation involves only a few major activities, which comprise nearly all of the work. For most of them the states already compile suitable data on the volume of work performed. With a revision of the accounting systems, it would be feasible for the agencies to set up their expenditures by activities and to determine unit costs. It would then be possible for them to base their budget requests on definite estimates of work load for the coming period and on unit costs derived from previous experience. This should simplify the preparation of the budget and help state officials to justify their requests. At the same time, it would help the Bureau of Employment Security to judge the validity of the estimates and determine the amount of the grant required. This method of budgeting would also bring into clear relief the high- and low-cost agencies. Special studies could then be undertaken to determine the factors responsible for these costs, and the results could be used to raise the efficiency of unemployment compensation administration throughout the country.

The central office of a state agency and its local employment office system present considerably different problems in budgeting. Apart from



the staff and service units, which account for only a small part of the cost, the work of the central office consists almost entirely of a few highly routine unemployment compensation activities for which unit costs could be established without especial difficulty. The work load for these activities is almost entirely determined by conditions outside the control of the agency. Persons become unemployed and claim benefits; the agency must then determine their claims and, if they are eligible, pay benefits. When unemployment decreases or claimants have exhausted their benefit rights, the volume of activity declines. The same is true of the unemployment compensation activities of the local offices.

But in so far as the employment service function of the local office is concerned, standard costs scarcely exist. For example, it costs several times as much to register and place a technical person as it does a laundress or an agricultural worker. Likewise, it costs more to place a farm hand for a year-round job than a harvest worker. Consequently, unit costs have but limited value in analyzing local office expenditures. The volume of activity also depends largely on factors that are not readily measurable. While the number of placements varies in considerable degree with the condition of the labor market, it differs even more according to the energy and ability of the staff. The number actually made may be but a fraction of the number an effective office could make in the same community. All these considerations indicate that budgeting the needs of local employment offices requires greater exercise of personal judgment than estimating the expenses of the central office. The difference between central and local offices necessitates a somewhat different approach in budgeting.

### *Central Office Activities*

The operations of the central office of an employment security agency are particularly well adapted to budgeting by activities. Exclusive of the executive offices and the staff and service units, which can for convenience be grouped as administrative overhead,<sup>8</sup> the work of the central office falls within the following major activities:

1. Administration of contributions.
2. Collection of wage reports and maintenance of employee wage records.

<sup>8</sup> The usual overhead activities of a central office are direction and supervision of unemployment compensation and employment service, fiscal administration, personnel administration, legal affairs, research and statistics, and information service.

3. Determination of benefit claims.
4. Adjudication of appealed claims.
5. Payment of benefits.
6. Operation of employer experience rating.

The expenditures for the first purpose could be reduced to unit costs per employer reporting unit, while those for wage records and reporting could be converted into unit costs per 1,000 employee wage reports received.<sup>9</sup> Costs could be calculated for the third, fourth, and fifth classes of activities on the basis of the number of benefit claims, appeals, and payments, respectively. Expenditures for experience rating might require different treatment according to the experience rating system used, though annual expenditures could be reduced to cost per employer. For purposes of comparison, expenditures for administrative overhead could be shown as a percentage of total expenditures and as a cost per insured worker.

Though it would be feasible to distribute all central office expenditures by operating activities, to do so would greatly increase accounting work and would not provide information of more value to either the federal or the state agencies. The problem is not that of a manufacturer making a dozen different products. It is not necessary to determine the exact cost of each product including all cost factors, for there are no prices to be fixed and no questions of profit or loss to be resolved. Rather, the problem is to obtain an analysis of expenditures which will facilitate the preparation and review of budgets and the determination of grants and will throw light on the relative efficiency of state agencies. Such an analysis would probably be complicated, rather than aided, by distributing overhead to operating activities. Likewise, items such as rent of premises can more readily be examined and appraised if set up by office instead of being apportioned by activities.

Since personal services comprise four-fifths of the cost of unemployment compensation administration, it would be sufficient for budgetary purposes if the expenditures in this category were classified by activities, but it would also be desirable to have a similar breakdown of supplies, the rental and maintenance of equipment, and perhaps postage. It would not be necessary to apportion by activities items such as rent of premises,

<sup>9</sup> In states obtaining wage reports only at the time of separation, annual expenditures for wage records and reporting could be reduced to cost per first claim filed during the year. On this basis comparisons could be made between costs in states using wage and separation reports and those which rely on current reporting of wages.

travel, and telephone and telegraph service in order to obtain the type of analyses needed for budgets and grants. These expenditures could continue to be set up by categories with suitable supporting data. Equipment estimates should, of course, be itemized and rent shown by offices, as at present. In addition, there should be a detailed schedule breaking down personal services by organization units and classes of positions. If expenditures other than personal service were also distributed by activities, as hardly seems necessary, there should be a further division by expenditure categories to permit a type of analysis which would not be possible from an activities classification alone. The budget should, of course, include comparative data for the current and previous years, as well as estimates for the coming period.

An activities budget should be accompanied by a work program for the agency. In addition to explaining proposed changes in organization and procedure that might affect costs, the work program should include tables showing for each activity the number of units of work performed during a two- or three-year period, broken down by months, together with the estimated number for the period covered by the budget. There should also be an explanation of the method by which these estimates were produced and of the factors involved if they differ materially from previous experience.

Certain activities, such as contribution administration, are very stable and change but little from one quarter to another. For these, expenditure requirements can be calculated very closely. Benefit activities, on the other hand, are so variable and in a measure so unpredictable that they cannot be estimated accurately. Consequently, it would seem that the form of the budget and the method of making grants should be adjusted to this fact. If the estimates for unemployment compensation operations were set up by activities, it would be feasible to effect this adjustment. For the more fluctuating activities—particularly determination of claims and payment of benefits—it would be desirable to have estimates of the basic work load which the agency should be permanently staffed to handle, as well as estimates of the total volume of activities expected. It would then be possible to make grants for central office operations in two parts. One would be a basic grant to cover administrative overhead, contribution administration and other relatively stable activities, and the basic load of benefit activities, together with rent and other classes of expenditures not distributed by activities. The other part

would be a reserve grant to be available if the volume of work in the more fluctuating activities exceeded the basic load approved by the Board. The extent to which the reserve could be utilized might be limited by applying specified unit cost factors to the excess of the actual over the approved basic work load of the agency. The greater the excess, the greater would be the extent to which the agency could draw upon the reserve grant.

The basic grant for the central office of the state agency could either be made as a lump sum or be divided according to major activities and expenditure categories for items not set up by activities. A lump sum grant would seem preferable, as it would provide greater flexibility in the operation of the agency and would relieve the federal bureau of the necessity of passing upon numerous minor transfer requests. With better information on costs by which to judge the validity of budget requests and to appraise performance, less advance federal control need be exercised over the expenditure of grants. Experience, however, would seem to indicate the need for retaining the requirement of advance approval of major equipment expenditures. There is considerable temptation to purchase unnecessary equipment and make changes of equipment which may vitally affect the future operation of an agency.<sup>10</sup>

### *Local Office Activities*

It would be much more difficult to construct budgets by activities for local employment offices than for the central office of the state agency. Moreover, it is doubtful whether there would be any advantage in doing so. Valid unit costs would be very hard to determine, and they would differ widely among offices and within the same office between busy and slack seasons. Most employment offices have staffs of not over six persons, with each person engaged in several activities. In determining the staffing and expenditure needs of local offices, it is necessary to rely more on the judgment of the manager and experienced field supervisors than upon data produced from accounts. For employment offices, a budget set up by offices and expenditure categories is probably as satisfactory as any; but data on the volume of activities are helpful in reviewing the budget to determine whether an office should be retained and whether

<sup>10</sup> It is assumed that the Social Security Board would continue to pass upon classification plans and salary schedules and that expenditures for personal services would have to conform to them.

the number of personnel bears a reasonable relation to the amount of work performed, with due consideration of the type of office.<sup>11</sup>

There is even more need of lump sum grants for the local office system than for the central office. Segregation by offices is impracticable because of the extreme fluctuations in the work of employment offices and the necessity of opening new offices at times and shifting personnel from one area to another. Nor is it particularly worth while to divide the grant for local offices by expenditure categories, as personal services represent more than 80 per cent of the whole. At most, a division into personal services, other current expenses, and equipment should be sufficient, and a lump amount should be feasible.

In summary, the plan discussed above would involve the separation of budgets for the central office of a state agency and for the local offices. The former would divide personal services and a few other classes of expenditures into administrative overhead and about half a dozen major operating activities and would set up other classes of expenditures by expenditure categories. The local offices budget would be broken down by offices and expenditure categories. Both budgets would be supported by a work program and detailed schedules for personal services. For the central office, the work program would consist of estimates of work load for each activity for the coming year, and, for local offices, an analysis of activities for the past year with a statement of proposed changes of program for the coming year. On the basis of these budgets, the federal grant under the Social Security Act would be made in lump sum form with a separation between central and local offices. The grant for the central office would be divided into a basic grant to meet ordinary needs and a reserve grant to take care of the excess of the actual work load over the basic work load for which the agency should be permanently staffed.

<sup>11</sup> The British Ministry of Labour has developed a formula, known as the staffing basis scheme, by which it determines the number of personnel required by local offices for unemployment insurance work according to the volume of activity. The formula, however, does not apply to placement activities.

## CHAPTER VI

### FEDERAL STANDARDS OF ADMINISTRATION

THE SOCIAL SECURITY BOARD, more than any other federal agency, is exerting a powerful influence upon the character of state government. While the Board's supervision applies only to the agencies conducting the employment security and public assistance programs, its efforts in these fields are beginning to affect the general level of state administration. Already the regulations which it has prepared on purchasing methods and the control of travel expenses have been adopted by several states for the administration as a whole. In most states the merit system established for employment security personnel represents the first application of civil service to state employment.<sup>1</sup> Undoubtedly, in many it is the entering wedge for the eventual adoption of a general state system of civil service.

#### NEED FOR ADMINISTRATIVE STANDARDS

Early in its dealings with the states the Social Security Board discovered that many did not conform to well-recognized principles of efficient practice in various aspects of their administration. Only nine had civil service for the selection of personnel, and in several of these its operation was seriously defective.<sup>2</sup> Nearly half made little or no provision for centralized purchasing and some placed very few safeguards about the purchasing process. Many lacked modern systems of accounting and expenditure control. Relatively few could be said to have effective regulations and procedures in all of these fields.

To assure proper administration of the employment security program in the absence of adequate state methods and controls, the Social Security Board has developed a considerable body of minimum standards with which state agencies must comply to qualify for federal grants.

<sup>1</sup> In most states the employment service personnel was brought under the merit system before it was applied to unemployment compensation employees. The United States Employment Service began the introduction of a merit system for state employment services in 1934, a year preceding the adoption of the Social Security Act.

<sup>2</sup> This is the number of states with civil service in 1936. By 1940 the number had risen to 16.

Most of these standards relate to basic administrative procedures, particularly those having to do with fiscal and personnel administration, procurement, and property control. To assist the states in meeting these requirements, the Board has drafted model regulations and plans of procedure suited to the needs of employment security agencies. While the adoption of these drafts is not mandatory, most agencies whose regulations and procedures did not conform to federal standards have accepted the drafts either in toto or in large part.

The establishment of sound minimum standards of administration is basic to the effective operation of the federal-state system of unemployment compensation and employment service. Years of governmental experience have produced a considerable body of principles and procedures, the application of which has been found to contribute to efficient public administration. To ignore them would be to leave the door open for waste and a possible breakdown of the enterprise in some areas. In calling for their observance, the Social Security Board has only been asking states to adhere to methods which the federal government and many of the more progressive state and local governments have already adopted of their own volition. In insisting, for example, upon the merit system for the selection of personnel and upon competitive bidding in purchasing, the Board is in reality protecting the state administrator from undesirable pressures and helping him to do a better job in the conduct of his agency.

With complete federal financing of administrative expenses, there can be no question either of the desirability or of the right of the federal government to establish suitable standards of administrative practice. But even if the state were required to match the federal grant, they should be applied. No state is entitled to receive federal money unless it is willing to use it efficiently. The taxpayers of the country have a right to expect no less, and Congress and the federal agency in charge of grants have an obligation to see that reasonable standards of administration are observed. To the extent that such standards are maintained, the need of close supervision is reduced. This lightens the task of the federal agency and allows the states greater freedom in the operation of the enterprise. There is ample evidence in the employment security program that, in general, the higher the quality of state administration, the less rigid is the federal inspection and the greater is the reliance of the federal agency upon the judgment of the state administrator.

### AUTHORITY FOR ADOPTION OF STANDARDS

Whereas the Wagner-Peyser Act specifically provides for the establishment of minimum standards for the administration of employment service, the Social Security Act makes no definite provision for federal standards relating to the administration of unemployment compensation. Such powers as the Board possesses are derived from the requirement of section 303(a) that the state "law" shall provide for "such methods of administration . . . as are found by the Board to be reasonably calculated to insure full payment of unemployment compensation when due," and that of section 302 that it shall grant such amounts as it "determines to be necessary for the proper and efficient administration of such law."

While more definite language would be desirable, the combination of the two sections affords an adequate basis for the establishment of administrative standards. Clearly, the Board cannot determine the cost of proper and efficient administration without defining what it constitutes. Whether the tests of proper administration are reduced to writing and issued to the states or are carried in the heads of the federal staff, the Act presumes their existence and application. If tests exist, it is only fair that the states know them so that they may adjust the administration of their agencies accordingly.

### EVOLUTION OF ADMINISTRATIVE STANDARDS

Apart from a few requirements included among the tests of conformity applied when approving state laws, the early development of administrative standards centered about the making of grants. It soon became necessary to prescribe the form of the budget and the main features of the budget procedure. These, together with the financial reporting requirements, fixed the main outlines of the administrative accounts of state agencies and provided the foundation for their systems of fiscal administration. The review of budgets raised questions on the kinds of expenditures which came within the proper administration of unemployment compensation and might be financed from federal grants. These questions led to the development of a body of policies on allowable expenditures, which amounts to a set of federal expenditure regulations for the state agencies.

With these exceptions, it is somewhat difficult to determine the administrative requirements laid down by the Board during the first few years.



Statements of policy were frequently couched in language which left it uncertain whether they were mandatory or advisory. In fact, the term "standard" was, and still is, used rather loosely to signify either a regulation or a recommendation on good practice. This ambiguity arose in part from uncertainty as to the extent of the Board's authority and from the necessity that the Board feel its way along in a new enterprise and a unique kind of federal-state relationship. On many questions, even of fundamental importance, answers could not be given with any assurance at that stage in the program. In a few cases decisions which took the form of definite requirements were completely changed within a few months. To cite a case: in the spring of 1937 the Board prescribed monthly collection of contributions, and later in the year it authorized quarterly collection.

In 1938 the Board began the preparation of a body of administrative standards. Certain of these standards were definite regulations for all agencies, and others, such as the original merit system standards, were conditions for the substitution of grants by expenditure categories for the more itemized form of grant. These standards are now set forth in two documents, one dealing with the merit system and the other with fiscal affairs, procurement, and a few other aspects of administration.<sup>3</sup> While these documents codify a large part of the administrative regulations of the Board, there are also many statements of policy scattered among minutes of the Board, letters to the states and the regional representatives, and decisions in specific cases, with which compliance is expected.

### FISCAL STANDARDS

The Board's instructions on fiscal affairs, generally referred to as Instructions ES-501, cover a considerable range of fiscal and business practices. The original purpose of these instructions was to set up the basic rules concerning budgets and grants, but they have been expanded to include other aspects of business management. As the regulations and procedures directly relating to budgets and grants have been considered in the preceding chapter, they need not be reviewed at this point.

<sup>3</sup> Social Security Board, *Standards for a Merit System of Personnel in State Employment Security and State Public Assistance Agencies*, November 1939; and *Instructions to State Agencies Relative to Fiscal Affairs in Connection with Grants Made for Expenses of Unemployment Compensation and Employment Service Administration*, Instructions ES-501, September 1939.

### *Accounting and Expenditure Control*

Instructions ES-501 set forth a number of expenditure regulations, but do not provide a definite system of expenditure control. They prescribe the expenditure classification to be used in budgets and financial reports and require the maintenance of a system of accounts which will adequately supply the information required for the reports, but they do not set up a standard accounting system for state agencies. In practice, however, the accounts of most agencies have been built almost entirely around the Board's reporting requirements. To aid the states in meeting these requirements, the Board has developed a plan of accounts which many of the agencies have largely adopted.<sup>4</sup> Prior to transfer to the Social Security Board, the United States Employment Service had also prepared a system of accounts for state employment services, which has been very generally used for employment office expenditures.

Existing reporting requirements call for accounts on an accrual basis set up by central and local offices, with a breakdown for each office by categories according to the federal expenditure classification.<sup>5</sup> It is not necessary for reporting purposes to segregate expenditures by organization units within the central office, and very few agencies have done so. Neither have expenditures been shown by activities, but plans are being prepared for obtaining this breakdown.

Considerable revision is necessary if the accounts of the agencies are to produce information of maximum value either from the standpoint of financial reporting or of expenditure control. For purposes of cost analysis and comparison among states and different fiscal periods, a breakdown of central office expenditures by major activities is needed so that expenditures may be related to volume of work performed. For purposes of financial control—at least in the larger states—a classification of central office expenditures either by activities or by principal organization units would be desirable. As the organization of the office roughly corresponds to the principal activities, a classification by activities would satisfy reasonably well the needs of both the Board and the agency for comparative cost information and the requirements of the agency for effective expenditure control. With such a breakdown properly keyed in with reports on the volume of activities, the agency could watch its

<sup>4</sup> Social Security Board, Bureau of Accounts and Audits, *Suggested Manual of Accounts for a State Unemployment Compensation Agency*.

<sup>5</sup> See footnote on page 61 for this classification. Expenditures for supplies, telegraph service, postage, transportation of things, printing and binding, and advertising are not broken down by employment offices.

costs and exercise a much more effective control over expenditures. If this change were made, the adoption of a standard system of accounts would be very desirable, as a large part of the value of a classification of expenditures by activities depends upon the comparability of expenditure data among states.<sup>6</sup>

So long as grants were made by quarters and in a highly segregated form, there was no need of requiring agencies to make a further allocation of their resources for purposes of financial control. The approved budget was in effect a detailed schedule of allotments. But with the change from quarterly to semi-annual (and perhaps eventually annual) budgeting and from itemized to lump sum grants, an allotment system becomes important to effective planning and control. Semi-annual (and even more, annual) grants need to be allocated either by months or quarters and according to activities or organization units. No doubt many of the states will adopt this practice of their own accord, for it involves little more than the continuance of a type of detailed financial planning that has been required in the past by the form of the grant and the brevity of the fiscal period. But a federal standard requiring an allotment system would help to assure the practice.

### *Expenditure Regulations*

The expenditures of employment security agencies are governed, of course, by state expenditure regulations in so far as they exist. Because of the inadequacy of these regulations in some states and the necessity of preventing the use of federal grants for purposes not within the scope of unemployment compensation and employment service, the Board has imposed a number of restrictions on the expenditure of the funds it supplies. One of the most basic of these limitations is the policy that grants will not be made or expenditures allowed for any state administrative unit other than the employment security agency itself, unless the unit customarily depends on fees or service charges for its support or performs work which normally is carried on by employment security agencies for themselves. This rule ordinarily bars payments for the extra expenses of central administrative offices, such as those of the attorney general, the comptroller, and the treasurer, incurred in performing for the employment security program their usual functions. On the other hand, if the treasurer participates directly in the benefit payment process by issuing

<sup>6</sup> For the reasons indicated in the preceding chapter, it probably would not be worth while to set up local office expenditures by activities. A classification by offices and expenditure categories would be more practicable and would be sufficient for financial control.

the benefit checks, or if the attorney general assigns a representative to the agency to handle employer liability questions, the cost may be paid from the federal grant. In the case of civil service commissions, the Board has departed somewhat from this general policy in order to remove financial obstacles that might impede the application of the merit system to employment security personnel. Numerous lesser restrictions are to be found among the fiscal instructions and policies of the Board. For example, automobile purchases are limited to a price of not over \$750 f.o.b.; the payment of sales taxes is barred; and the purchase of insurance is not allowed except where there is unusual risk.

The Board has also adopted definite standards governing travel expenses in order to systematize the handling of this matter and avoid excessive expenditures.<sup>7</sup> To be reimbursable, travel must be properly authorized and limited to official business. Except for the head of the state agency, out-of-state travel requires advance approval by the regional representative. The state may compensate employees for subsistence away from their official stations either at a flat per diem rate, as the federal government does, or at actual cost subject to a fixed limit per day. A definite mileage rate is required when employees use their own automobiles. If the state has general regulations adequately meeting these standards, that is sufficient. Otherwise, the agency must adopt regulations of its own. In most states, existing general regulations have required some supplementation, and in many a complete set of travel regulations has had to be adopted by the agency. Most agencies have modeled their regulations to a large degree after a draft prepared by the Board.<sup>8</sup> Where existing state laws and regulations do not prescribe a maximum limitation on subsistence, the limits adopted by the agency require the approval of the Board. Normally, it will not approve subsistence rates of more than \$5 per day for intrastate travel. The travel standards were originally adopted in the summer of 1938 and have now been met by nearly all states.

<sup>7</sup> Instructions ES-501, Nos. 4140-244. There have been some obvious cases of abuse in charging travel expenditures. In one state, members of a full-time unemployment compensation commission charged the agency for their regular travel between their homes and the office of the agency. In another, the head of the agency presented a bill for \$100 for two days' subsistence. These, of course, are exceptional cases, but they illustrate the need for travel regulations.

<sup>8</sup> Social Security Board, Bureau of Employment Security, "Draft Travel Regulations Relating to Expenditure of Funds Granted by the Board Pursuant to Title III of the Social Security Act and the Wagner-Peyser Act, for Travel Expenses of State Agencies Administering Unemployment Compensation and Employment Service," *Administrative Standards Bulletin*, No. 1.

### *Fund Management*

In cooperation with the states and the federal treasury, the Board has worked out an unusual plan for the management of unemployment compensation funds in the hands of the states. Each state has three funds: the administration fund consisting of the federal grant, the clearing fund to which contribution payments are credited pending deposit in the federal unemployment trust fund, and the benefit payment fund consisting of moneys withdrawn from the unemployment trust fund for the payment of compensation.<sup>9</sup> The second and third handle large amounts of money in the course of a year, and the third, in particular, has a vast number of individual transactions. To compensate the depository banks for handling the large numbers of checks passing through these funds, it was necessary for the states either to pay substantial bank service charges or to maintain large balances which drew no interest. The former meant an increased federal grant, and the latter, loss of considerable revenue inasmuch as reserves on deposit in the federal treasury's unemployment trust fund have been drawing 2½ per cent interest.

To reduce the carrying charges on the funds and enable the states to obtain the maximum return on their unemployment compensation reserves, the United States Treasury Department has offered to maintain sufficient federal deposits in the banks handling the state funds to compensate them for their services, provided the banks qualify as federal depositories. To meet the requirements of the Treasury Department, the funds must be deposited in banks which are members of the Federal Reserve System and be kept separate from other state moneys.<sup>10</sup> The Treasury Department obtains reports of the daily balances and the volume of checks handled by each depository and adjusts its deposits of federal moneys according to carefully determined rules for compensating bank services. This method of paying for bank service, which is the one used by the federal government for its own accounts, is known as the compensating balance plan.

Since the development of this arrangement, the Social Security Board has discontinued grants for the payment of bank service charges and has instituted closer supervision of fund management in the states to see

<sup>9</sup> These funds are commonly referred to as accounts, but are generally managed as separate funds.

<sup>10</sup> In addition, the Social Security Board is giving some attention to the protection of deposits by requiring state depositories to put up collateral and is urging that unemployment compensation funds be protected to the maximum degree provided by state depository laws.

that moneys in clearing funds are promptly deposited in the unemployment trust fund where they draw interest, and that withdrawals are made from the trust fund only as actually needed to pay benefits. By means of the compensating balance plan and better fund management, the cost of maintaining unemployment compensation funds has been reduced and the interest earned on reserves has been substantially increased. When the plan is in full operation, it is estimated that it will yield the unemployment compensation system at least \$85,000 a month in additional depository interest<sup>11</sup> and will involve considerably lower cost for the federal government than would the payment of grants to cover bank service charges on state unemployment compensation funds.

#### STANDARDS OF PROCUREMENT AND PROPERTY CONTROL

Purchasing constituted an especially important problem during the first three years of the unemployment compensation program. In comparison with foreign unemployment insurance systems, the American state systems involve an unusually great amount of centralized and highly mechanized record work, and therefore initially required large equipment purchases. In the beginning there was great danger that some of the agencies might misjudge their requirements and obligate themselves for excessive amounts and inappropriate or needlessly costly types of equipment, as well as some over-elaborate furniture. Also there has been a tendency for some agencies to seek to shift from one type of equipment to another, often without sufficient consideration of their relative merits and the cost of the change. These conditions early led the Social Security Board to require prior federal approval of equipment purchases, which usually is given through the budget.

In addition, the Board has had the problem of preventing states from diverting to other departments equipment purchased from federal grants for employment security administration. In consequence, it has required agencies to keep complete inventories of their equipment and to send copies to Washington, together with periodic lists of new items, from which the Board maintains a record of each agency's equipment and makes test checks of the inventory in connection with audits. While the equipment is legally state property, the Board considers it to be held in

<sup>11</sup> The depository interest is credited to the state's account in the unemployment trust fund and does not increase the money available for administrative expenses.

trust for employment security administration and therefore insists that agencies obtain federal approval before disposing of any of it.

Looking to the elimination of prior approval of most equipment purchases, the Board has developed a list of the standard equipment used by state agencies and a set of model specifications providing a suitable grade for each item. The list and the specifications represent more than three-fourths of the equipment acquired by the agencies in terms of cost and cover most of their needs exclusive of office machinery. The specifications drafted by the Board are advisory rather than mandatory. Upon adoption of state specifications meeting the Board's approval, lump grants are made for the purchase of any equipment included in the standard list, assuming, however, that the state procurement procedures satisfy the Board's standards.

In the fall of 1939 the Board issued a set of minimum standards on procurement and a suggested draft of procurement regulations for agencies not covered by state purchasing provisions meeting these requirements.<sup>12</sup> The standards recognize three possible situations. Where the state law so requires, purchases for the employment security agency are to be made through the central purchasing office, but the procedures employed in handling these purchases must conform substantially to the Board's standards. Where the state maintains, but does not compel the use of, centralized purchasing facilities and they are readily available and comply at least in part with the federal standards, the agency is to utilize these facilities and supplement them with any additional controls needed to meet the Board's regulations. Where there is no centralized purchasing machinery or it is not readily available, the agency has to adopt suitable purchasing regulations and procedures of its own.

The procurement standards provide that all purchases shall be made on a competitive basis. The agency must advertise annually, inviting interested dealers to file their names for inclusion in its lists of vendors. Individual purchases amounting to \$1,000 or more have to be advertised in a newspaper of state-wide circulation. On those between \$50 and \$1,000, invitations for bids must be submitted to the dealers on the appropriate list of vendors. Where the amount is under \$50, prices must be obtained from at least three concerns. Bids are to be opened in public and recorded, and awards are to be made to the lowest responsible bidder. As with other standards, the Board has prepared a set of regulations for the guidance of agencies which have to establish their own purchasing

<sup>12</sup> Instructions ES-501, Nos. 4250-320.

that moneys in clearing funds are promptly deposited in the unemployment trust fund where they draw interest, and that withdrawals are made from the trust fund only as actually needed to pay benefits. By means of the compensating balance plan and better fund management, the cost of maintaining unemployment compensation funds has been reduced and the interest earned on reserves has been substantially increased. When the plan is in full operation, it is estimated that it will yield the unemployment compensation system at least \$85,000 a month in additional depository interest<sup>11</sup> and will involve considerably lower cost for the federal government than would the payment of grants to cover bank service charges on state unemployment compensation funds.

#### STANDARDS OF PROCUREMENT AND PROPERTY CONTROL

Purchasing constituted an especially important problem during the first three years of the unemployment compensation program. In comparison with foreign unemployment insurance systems, the American state systems involve an unusually great amount of centralized and highly mechanized record work, and therefore initially required large equipment purchases. In the beginning there was great danger that some of the agencies might misjudge their requirements and obligate themselves for excessive amounts and inappropriate or needlessly costly types of equipment, as well as some over-elaborate furniture. Also there has been a tendency for some agencies to seek to shift from one type of equipment to another, often without sufficient consideration of their relative merits and the cost of the change. These conditions early led the Social Security Board to require prior federal approval of equipment purchases, which usually is given through the budget.

In addition, the Board has had the problem of preventing states from diverting to other departments equipment purchased from federal grants for employment security administration. In consequence, it has required agencies to keep complete inventories of their equipment and to send copies to Washington, together with periodic lists of new items, from which the Board maintains a record of each agency's equipment and makes test checks of the inventory in connection with audits. While the equipment is legally state property, the Board considers it to be held in

<sup>11</sup> The depository interest is credited to the state's account in the unemployment trust fund and does not increase the money available for administrative expenses.



trust for employment security administration and therefore insists that agencies obtain federal approval before disposing of any of it.

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<sup>12</sup> Instructions ES-501, Nos. 4250-320.

systems.<sup>13</sup> Though the procurement standards were not issued until the fall of 1939, by September 1940 thirty-five states had either adjusted their centralized purchasing procedures or had adopted special purchasing systems for their employment security agencies in substantial conformity with the federal standards. Twelve of these states had special systems and twenty-three used centralized purchasing facilities.

With more than 1,600 employment offices, housing presents another important aspect of employment security administration, both because of the rental cost and the effect of office quarters on operating efficiency. In a number of states, including some of the largest, the conduct of unemployment compensation is severely handicapped by cramped or badly arranged central offices. Many local offices also suffer from unsatisfactory housing. In some communities suitable quarters simply are not obtainable. This is especially true of central offices in populous states with capitals in small cities. The Board has given considerable attention to the amount of space required for various types of offices and some to office layout. Thus far the federal agency has mainly interested itself in the financial aspects of office quarters. It regularly reviews the terms of leases and proposals for repairs and alterations, but this review is mainly to forestall unnecessary expenditures and to see that agencies avoid undesirable contractual obligations. Long-term leases are frowned upon and thirty-day cancellation clauses are urged, owing to the impossibility of forecasting normal needs at the present stage in the program. Only a few standards have yet been developed relating to quarters.

### PERSONNEL STANDARDS

More far-reaching than the fiscal standards of the Board are its efforts in the field of personnel administration. It was recognized from the outset that the success of a federal-state system of unemployment compensation would depend in large measure upon the caliber and training of the state personnel charged with its administration. If the staffs of the agencies were recruited on a patronage basis and subject to turnover with each change of administration, it was apparent that the system would soon break down and unemployment compensation be discredited. The realization of these dangers led the President's Committee on Economic

<sup>13</sup> Social Security Board, Bureau of Employment Security, "A Draft Regulation Relating to Procurement of Furniture, Fixtures, Equipment, Supplies, Printing and Binding, and Contractual Services by State Agencies Administering Unemployment Compensation and Employment Service," *Administrative Standards Bulletin*, No. 2, 1939.

Security to recommend that the federal act require high administrative standards and that the personnel of state agencies be selected on a merit basis.<sup>14</sup>

### *Legal Basis for Merit System Standards*

In promoting effective methods of personnel administration, the Board labored under a serious legal handicap until 1940. In accordance with the recommendations of the President's Committee, the Wagner-Lewis Bill, which became the Social Security Act, originally provided as a condition of federal grants to any state that the Board must find that "all positions in the administration of the unemployment compensation law of such state are filled by persons appointed on a non-partisan basis, and selected on the basis of merit under rules and regulations prescribed or approved by the Board."<sup>15</sup> A combination of states' rights sentiment and partisan pressure in the Senate committee, however, swept this provision from the bill and inserted language intended to prevent the establishment of personnel standards. As finally enacted, the section which required state laws to provide for such methods of administration as the Board might find calculated to insure full payment of benefits when due, specifically excluded methods "relating to selection, tenure of office, and compensation of personnel."<sup>16</sup> The inconsistency and futility of attempting to assure effective administration of this or any other program while ignoring the type of personnel responsible for its operation are too apparent to need elaboration.

On the recommendation of the Board, this provision of the Social Security Act was amended in 1939 to require, after January 1, 1940, "methods [of administration] relating to the establishment and maintenance of personnel standards on a merit basis, except that the Board shall exercise no authority with respect to the selection, tenure of office, and compensation of any individual employed in accordance with such methods." This amendment gave the Board not only the authority needed to establish suitable personnel standards for state agencies, but a definite mandate to do so. It is interesting to observe that some of the congress-

<sup>14</sup> *Report of the President's Committee on Economic Security*, 1935, pp. 4, 18, 19.

<sup>15</sup> 74th Congress, 1st sess., S. 1130, Mr. Wagner, and H.R. 4142, Mr. Lewis, sec. 407.

<sup>16</sup> Until amended in 1939, the pertinent part of section 303(a) read:

"The Board shall make no certification for payment to any State unless it finds that the law of such State, approved by the Board under Title IX, includes provisions for:

"(1) Such methods of administration (other than those relating to selection, tenure of office, and compensation of personnel) as are found by the Board to be reasonably calculated to insure full payment of unemployment compensation when due."

men who were most opposed to these standards in 1935 were most insistent upon their adoption in 1939, after discovering that the patronage from social security grants went to governors rather than to themselves and in some cases was helping to build a rival political organization in the state.<sup>17</sup> This discovery undoubtedly contributed to an awakened consciousness of the value of the merit system.

### *Merit System of the United States Employment Service*

Though the Social Security Board was hampered by an inadequate law in its early efforts to improve personnel practices, it was considerably aided by the precedent of the merit system established by the United States Employment Service for state employment services. This was the pioneer application of the merit system to agencies supported by federal grants. Under the broad authority conferred by the Wagner-Peyser Act to fix minimum standards, the United States Employment Service adopted in 1934 a set of personnel regulations for state employment services. As later revised, these standards provided for the application of the civil service laws and regulations of the state if it had a civil service system and, if not, for selection from eligible lists based on examinations conducted within the state by the United States Employment Service itself.

For more than three-fourths of the states, these requirements involved the establishment of a special federally administered merit system for employment service personnel. Under this system the United States Employment Service prepared and graded the examinations at its office in Washington. The examinations were administered in the state by a local person designated by the federal bureau, usually from the faculty of the state university on the recommendation of its president. For existing employees the examinations were qualifying, as a rule, and for new personnel, competitive. The eligible lists were set up by the United States Employment Service, and appointments were reviewed by it for compliance with its personnel regulations. By the end of 1937 the employment service personnel had been brought under state civil service or this federally administered merit system in all but two states.<sup>18</sup>

<sup>17</sup> Some senators found governors seeking their seats and trying to use appointments in state social security agencies for political advantage.

<sup>18</sup> The merit system of the United States Employment Service is described in detail in Atkinson, Odenrantz, and Deming, *op. cit.*, Chapter 10. The regulations which governed the system are set forth in United States Employment Service, *Personnel Standards of the United States Employment Service*, July 1, 1938.

*Beginnings of the Merit System for Unemployment  
Compensation Personnel*

As the Social Security Board was prevented by its law from following the example of the United States Employment Service,<sup>19</sup> it focused its efforts on promoting adoption of the merit system by the states. Few states had their own civil service systems and it was necessary in most cases to seek the establishment of special systems for unemployment compensation agencies. A provision was inserted in the original Draft Bill requiring all positions in the agency to be filled by "persons selected and appointed on a nonpartisan merit basis."<sup>20</sup> Later this provision was revised to require the holding of examinations and the appointment of personnel "on the basis of efficiency and fitness as determined in such examinations."<sup>21</sup>

One or the other of these proposals was incorporated in the unemployment compensation laws of a majority of the states—in many, probably with little realization of the presence of the requirement. Once on the statute books, the provisions were useful levers for obtaining the actual establishment of merit systems. In a number of states the heads of the new agencies promptly recognized their obligation and readily accepted the Board's assistance in working out plans for the system.<sup>22</sup> In some others, where officials delayed or sought to evade the establishment of a merit system, the Board eventually took the position that the agency must comply with the requirements of the state law to obtain federal grants. Nevertheless, a few agencies with merit system provisions in their acts took no steps to effectuate them until after the 1939 amendment of the Social Security Act requiring the establishment of merit systems.

As state administrators began to realize the complexity of their enterprise and feel the pressure for political appointments, many recognized very clearly the need for careful selection of employees and protection

<sup>19</sup> The Social Security Board interpreted the limitation in section 303(a) to prevent the establishment of definite personnel requirements. It should be noted that this section dealt with requirements which must be satisfied by the state law as a condition of eligibility for grants. It is possible that the Board might have been able to establish personnel standards under the authority of section 302 providing for grants for the necessary cost of proper administration. It would seem that compliance with reasonable personnel standards would be one of the appropriate tests of proper administration. Part of the Board's standards of administrative practice are based on this provision.

<sup>20</sup> Social Security Board, *Draft Bills for State Unemployment Compensation of Pooled Fund and Employer Reserve Account Types*, January 1936, sec. 11(d).

<sup>21</sup> *Ibid.*, revised edition of January 1937, sec. 11(d).

<sup>22</sup> Kansas set up a merit system and held examinations within about three months after the agency was organized.

from the spoils system. The Interstate Conference of Unemployment Compensation Agencies, composed of the principal officers of the agencies, appointed a committee on personnel standards at one of its meetings in 1936, and subsequently created a technical committee which worked with representatives of the Social Security Board and the United States Employment Service in drafting regulations for a plan of personnel administration for state agencies, including a merit system.<sup>23</sup> While the recommendations of this committee were never adopted by the Conference, several regional conferences of state unemployment compensation officials passed resolutions recommending the establishment of merit systems.

Late in 1936 the Bureau of Unemployment Compensation issued a suggested plan of personnel procedure providing for a merit system, which was largely copied in several states.<sup>24</sup> The following year it was thoroughly revised with the aid of the personnel specialists of the Board, and a comprehensive set of regulations was prepared for the guidance of state agencies.<sup>25</sup> This draft, with various modifications, formed the basis for the original merit systems adopted by nearly half the agencies.<sup>26</sup> At about the same time, the Board created a special unit, known as the State Technical Advisory Service, to aid states in setting up personnel procedures and administering merit systems for unemployment compensation and public assistance agencies. This unit was staffed with persons experienced in examination construction and personnel administration. It has played a very large part in the development and installation of the merit system and orderly personnel procedures in the agencies. Most of the states, including several having their own civil service commissions, have used its services in classifying positions and formulating salary schedules and have relied heavily upon it for examination materials.

The first state to set up a special merit system for unemployment compensation personnel was Indiana, in the summer of 1936. In compliance with requirements in the laws creating the unemployment compensation agency and the state welfare department, these units jointly employed the Public Administration Service to assist them in formulat-

<sup>23</sup> Interstate Conference of Unemployment Compensation Agencies, *Report of Personnel Technical Committee*, October 1937.

<sup>24</sup> Social Security Board, Bureau of Unemployment Compensation, *A Plan of Personnel Procedure for a State Unemployment Compensation Agency*, November 1936.

<sup>25</sup> Social Security Board, *Draft of Regulations for Merit System and Personnel Administration in a State Unemployment Compensation Agency*, September 1937.

<sup>26</sup> The proposal of the Personnel Technical Committee of the Interstate Conference of Unemployment Compensation Agencies largely paralleled this draft.

ing a plan. The system established was unique in that it provided for a joint merit system conducted by a committee consisting of the directors of the two agencies concerned and a chairman appointed by them. The next state to act was Idaho in April 1937. In July, South Dakota and Washington adopted merit systems and in August, Alabama, Kansas, and Utah. These were followed by several other states before the end of the year. With the exception of Indiana the agencies, in general, followed the plan developed by the Bureau of Unemployment Compensation and largely depended upon the Board for the preparation of examination materials.

By the spring of 1939, the unemployment compensation personnel had been brought under a merit system in thirty-nine states. In eleven they were covered by state civil service and in twenty-eight by special merit systems for the unemployment compensation agencies. Nearly all of the twenty states which began the payment of benefits in 1939 held examinations in advance of the expansion of their staffs to handle this work, and selected the new personnel from eligible lists. Many of those which started benefit payment in January 1938, however, did not conduct their examinations in time to recruit their forces from merit system registers. When the registers later became available, some of these states experienced a heavy turnover in personnel, which caused considerable temporary difficulty in the operation of the agency. In a few states, as high as half or two-thirds of the employees had to be replaced, but as a rule most of the administrative and technical personnel survived the introduction of the merit system.<sup>27</sup>

### *Adoption of Merit System Standards*

In December 1938, the Board adopted definite personnel standards for unemployment compensation and public assistance agencies. Owing to the limitations of the Social Security Act, the standards were not mandatory, but the Board announced that for unemployment compensation agencies conforming to them it would discontinue the itemization of grants for personal services, thus giving the agencies much greater freedom in the use of funds. As personal services comprise by far the

<sup>27</sup> The high turnover in routine personnel was partly due to the fact that in some states the expansion of the force occurred between the date of the examinations and the time the eligible lists became available. Hence, many of the temporary employees had not taken the examinations. A few states apparently delayed their examinations to permit temporary and provisional appointments and later had considerable trouble due to high turnover during the early period of benefit payment.

greater part of the cost of unemployment compensation administration, this meant a substantial relaxation of detailed federal control. In 1939, following the amendment of the Social Security Act making the merit system mandatory, the Board adopted a new set of standards with which compliance was required.<sup>28</sup> By July 1940, nearly all the state employment security agencies had adopted regulations providing for a merit system in accordance with the federal requirements.

Though many of the agencies have not objected to the establishment of the merit system and some have welcomed it as a means of curbing political pressure and obtaining a more stable and better qualified staff, a number have resisted strenuously. No other matter has created as difficult federal-state relations as the campaign for the adoption of the merit system. In several cases, governors and congressmen have attempted to stave off its adoption, or to block the conduct of examinations or the use of eligible lists after adoption. One state enacted a sham civil service law to forestall the introduction of a real merit system for unemployment compensation personnel.<sup>29</sup> Only a few days before examinations were to be held, another passed an act providing that existing employees could be retained without examination. In a third state, where a change of administration occurred before the eligible lists were completed, the new governor prevented appointments from the registers for several months on the pretext that the examinations had not been properly administered. One of the first of the special merit systems came within a hair's breadth of repeal on the closing day of the next session of the legislature after its introduction.

Nearly a dozen agencies did not adopt merit systems until after the Social Security Act was amended in 1939. Several of them did not accept the Board's personnel standards until the payment of grants was suspended on February 1, 1940, apparently having waited to see whether the new requirements would be enforced. Up to that time the Board did not actually withhold payments for failure to establish a merit system, though it did apply considerable pressure in some cases and in a few instances informed states that money would not be granted to pay the salaries of persons appointed or retained in violation of personnel regulations already adopted by the agencies.

<sup>28</sup> Social Security Board, *Standards for a Merit System of Personnel Administration in State Employment Security and State Public Assistance Agencies*, November 1939.

<sup>29</sup> When it was pointed out to the head of the state agency that this so-called civil service bill lacked "any real teeth," he replied, "But you will have to admit that it has a good set of false teeth."



Once the system was installed and the initial changes of personnel were made, objection soon died out, as a rule. Those executives who themselves are under the merit system appear to be thankful for its existence, and a number of others wish that their laws permitted its extension to their positions. When viewed against state political traditions, the astounding thing is that the merit system has been applied to the agencies in so short a time and with no greater strain upon federal-state relations than has occurred. It is also interesting to note that the merit system program of the Board was not criticized during the 1940 session of Congress, despite the fact that the payment of grants was delayed in many states at the opening of the year until acceptance of the merit system was pledged.

#### *Principal Provisions of Personnel Standards*

The Board's standards are brief but cover in general language most of the fundamentals of a merit system. They apply to all positions in state employment security agencies other than the executive head, the attorneys, members of advisory councils, employer and employee representatives on appeals tribunals, and confidential secretaries to exempt officials. If the agency is headed by a full-time commission, its members are exempt, but the executive officer of the commission is subject to the merit system. If the state has a civil service system operating under standards substantially equivalent to those of the Board, it applies to the agency. Otherwise, the agency must establish a merit system of its own or create a joint system with other state agencies receiving social security grants. The merit system is to be administered by a council and a supervisor.

All positions must be classified according to duties and responsibilities and a compensation plan must be adopted establishing the salary range for each class of positions on the basis of prevailing rates for similar positions in the state service and other relevant factors. The classification and compensation plans require Board approval. Except for the exemptions indicated above, all positions must be filled in accordance with merit system regulations adopted by the agency or the state civil service authority. Open competitive examinations are required for entrance into the service, but qualifying examinations may be used for incumbents. Examinations are to be administered by the merit system supervisor and are normally to consist of a written test, a rating of training and experience, and, for administrative positions and those involving frequent con-

tact with the public, an oral interview. The supervisor is to score the examinations, prepare the eligible lists, and certify names from the lists for appointment. Provisional appointments may be made in the absence of an appropriate list, provided the supervisor finds that the minimum qualifications for the position are met. A probationary period is required. Removals may only be made for cause, and the employee has the right of appeal to an impartial body created by the merit system regulations. Political activity is prohibited. Standards have also been issued laying down a few principles on salary adjustment, vacations, and sick leave and requiring agencies to adopt definite rules thereon if they are not covered by suitable state regulations.

The standards do not constitute a complete set of civil service regulations; nor do they cover some points of considerable importance in setting up a merit system. For example, they do not fix a definite limit on the number of names to be certified to an appointing officer, or the maximum duration of provisional appointments. They are silent on temporary and emergency appointments, which are numerous because of the extreme fluctuations in unemployment compensation activity. While personnel records are required, their nature is not indicated. In approving state regulations, the Board, however, has insisted upon suitable provisions on such points. After receiving regulations from a few states providing for a greater number, it has ruled that not more than three names may be certified for a single position. One state proposed the certification of the entire eligible list for certain positions.

While establishing requirements adequate to assure a genuine merit system, the Board has tried to leave a reasonable degree of discretion to the states. There can, of course, be considerable differences of opinion as to the exact form a merit system should take. Certain of the Board's standards may for that reason be viewed as too specific and restrictive. Yet the fact has to be recognized that most of the state agencies are unfamiliar with problems of civil service administration and need guidance. Also, the standards cannot be too loose and flexible if the objectives of the merit system are to be achieved. Moreover, in applying federal standards, substantial rather than exact conformity is normally required. Definiteness is more essential in dealing with personnel practices than with any other phase of agency administration because of the greater political interest in evasion.

The Board has prepared a complete set of merit system regulations suitable for state adoption. They elaborate and apply the principles em-

bodied in the standards and cover in detail the points customarily treated in civil service laws and regulations.<sup>30</sup> The regulations provide for an unpaid merit system council composed of three members appointed by the agency, or agencies, for overlapping terms. The council is mainly an advisory body. The actual administration of the system rests with the supervisor appointed by the agency, or agencies, on recommendation of the council. The supervisor is primarily responsible for the examinations, the maintenance of eligible lists, the certification of names from the lists, and for the supervision of provisional appointments, promotions, etc., to see that the rules of the merit system are observed by the agencies. Each agency designates its own personnel officer and adopts classification and compensation plans for the positions in its employ, after review by the council. It is contemplated that the supervisor will be a part-time officer in most states, even where a merit system is established jointly for employment security and public assistance. The aim is to give the supervisor and the council an independent status and to keep the administration of the merit system largely distinct from the internal personnel activities of the agencies. In this, the plan follows the traditional civil service pattern. For the most part the states which do not have their own civil service have followed the Board's suggested regulations rather closely in setting up their merit systems.

### *Operation of the Merit System*

The supervisors, on whom the success of the merit systems depends to a great degree, have generally been selected from the faculties of local universities and colleges. More often than not, they have come from political science, business administration, or psychology departments. A number of the original group of supervisors had assisted in the operation of the merit system conducted by the United States Employment Service. With few exceptions the supervisors have been competent, thoroughly reliable, and interested in the success of the undertaking; but most have had little or no previous experience in civil service administration. Consequently, the Board throughout has had to supply a large amount of technical assistance. As a guide, an elaborate manual has been prepared which covers most aspects of the merit system and of personnel administration. Before undertaking an examination program, a new supervisor is invited to Washington and given from one to two weeks of training by

<sup>30</sup> Social Security Board, *Draft of a Rule for a Merit System of Personnel Administration in State Employment Security and State Public Assistance Agencies*, November 1939.

ance from a few state agencies which have already attained a relatively high level of efficiency and thus have been little affected by the standards adopted.

The 100 per cent grant has been both an advantage and a disadvantage in seeking to obtain compliance with federal regulations. While it has made the agencies unusually conscious of their financial dependence on the Board, it has prevented the Board from charging to state funds expenditures made in violation of standards. To far too great a degree, the Board has had to resort to threats of withholding grants to correct relatively minor deficiencies in compliance.

Yet the problem of acceptance of federal standards has not proved insurmountable by any means. The effectuation of new methods necessarily takes time. Except for the merit system, which runs counter to deep-seated political traditions, most of the administrative requirements of the Board have met little serious resistance. If the standards are fair and reasonable and not unnecessarily rigid, and if they are properly presented and their desirability well supported by evidence, the agencies are generally cooperative.

The first step in obtaining compliance with federal standards is proper preparation of the standards themselves. Experience has indicated the desirability of consulting regional representatives and state officials before the adoption of standards. Not only does this tend to avoid impractical and inappropriate provisions, but it assures better acceptance by the states. The field staff and the key personnel of the agencies have a knowledge of local operating problems and state attitudes which is needed in formulating plans and regulations to be applied in the states. Consultation with state statisticians, for example, has helped in developing a workable system of statistical reporting. In 1939 the review of the revised fiscal instructions by a group of state officials before adoption by the Board undoubtedly improved the reception they received in the states. It would seem that the use of advisory committees of state officials, selected for their acquaintance with the particular subject, would be a desirable regular technique in the preparation of standards.

It is also important that standards be clearly stated and that regulations and recommendations be definitely distinguished. Many of the early instructions and declarations of policy were so worded as to leave doubt whether compliance was necessary. Consequently, agencies which were inclined to be independent did nothing about them, and those which

adjusted their practices to conform sometimes felt they had been imposed upon when they later discovered the provisions were not mandatory. Diplomacy at times tended toward ambiguity. Recently issued standards have been much more definitely stated and have usually indicated whether or not they are mandatory.

Education and technical service ordinarily play the major part in making federal standards really effective. The agencies must understand the desirability of the new provision and how to apply it if it is to achieve its purpose. Most of the educational work has usually fallen to the regional representatives, but frequently the aid of technical specialists has been necessary in carrying out the standards. The work of the State Technical Advisory Service in helping agencies to formulate classification and compensation plans and install the merit system has already been described. The statistical staff of the Bureau of Employment Security has likewise advised states on procedures for obtaining the data needed for statistical reporting, and the Board's accountants have helped to develop accounting systems to meet budgetary and financial reporting requirements.

Behind education and technical service is the review of budgets, the audit of state operations, and the power to withhold funds. In the revision of budgets the Board eliminates so far as possible items not in conformity with federal standards, and in the audit of finances it disallows expenditures contrary to standards and the approved budget.

The Board maintains three general types of audits. The first is a periodic examination of the accounts of the agencies, usually at intervals of six months. This audit covers in detail the use of grants for administrative expenses, but does not include the clearing and benefit payment funds. These are viewed as strictly state funds to be audited by state authorities, but in practice few states are actually auditing them. Unless the states assume this responsibility, it will no doubt become necessary for the Board to examine the transactions of these funds on a sampling basis. A periodic audit of personnel activities is also being established to assure observance of the personnel standards. This audit will check particularly for compliance with the rules of the merit system in the appointment and removal of employees and for adherence to the classification plan and salary schedule. The third type of audit—as yet but partly developed—is the survey of operations. Comprehensive surveys have been made in only a few states, but an extension of the practice is con-

templated. These surveys may be viewed as audits only in the broadest sense. Their primary purpose is to assist the states in perfecting their methods of operation. They bring to light both good and poor procedures and provide information by which the federal Bureau may appraise the relative efficiency of different methods.

The disallowance of expenditures not made in conformity to the Board's standards and the terms of the grant partially meets the need for an enforcement device less cumbersome and drastic than the withholding of funds. But, as the state provides no money for the administration of unemployment compensation, there is nothing from which the administration fund can be reimbursed for disallowed expenditures if they cannot be recovered from individuals. Items such as over-payments of salaries and travel expenses can usually be recovered if the person is still employed by the agency. Yet in some cases officials have persistently disregarded audit findings against them on the assumption that the Board could not or would not compel repayment. There have also been cases where positions stricken from the budget for two consecutive periods have been retained and have appeared in the succeeding period.

To make audit disallowances more effective, the Social Security Act was amended in 1939 to require states to provide, after July 1, 1941, for the replacement of moneys "expended for purposes other than, or in amounts in excess of, those found necessary by the Board for the proper administration" of the state law.<sup>34</sup> The implementation of this provision presents difficulties. A mere promise by the state to appropriate the necessary amounts at some future time to reimburse the administration fund of the agency may not be enough. More effective would be the requirement of a relatively small annual state appropriation—probably a fixed percentage of the previous year's administrative expenses—to reimburse the fund for expenditures disallowed and not otherwise recovered. The purpose would have been achieved more certainly if the grant for administrative expenses had originally been placed on a reimbursement basis instead of being paid as an advance. The states would then have had to appropriate in the aggregate perhaps \$25,000,000 to provide the capital for revolving funds for the initial payment of expenses, and the federal government would have reimbursed them for the cost of proper administration. Disallowance of expenditures would have reduced the capital of a state's fund and eventually have forced the ad-

<sup>34</sup> 53 *Stat. L.* 1379.

administrator to go to the legislature to have it restored. This would have had a salutary influence. At this date such a plan probably could not be instituted for unemployment compensation administration, but it merits consideration in setting up any new 100 per cent grants.

The basic sanction for obtaining observance of standards is withholding grants, but it is one that can seldom be invoked. As yet, grants for unemployment compensation administration have been definitely withdrawn in only one state and there for less than two months. During this period the agency practically ceased operation. The withholding of grants is a power which can be used only in extreme circumstances when the case is sufficiently clear to command popular and Congressional approval. But this does not mean that it is not an effective sanction in less aggravated cases. It resembles the power of the British House of Commons to withhold appropriations if the Cabinet fails to follow the dictates of the House. To use the power would upset the whole national administration; but the mere existence of the authority, coupled with its early use, has created a tradition which has rendered its further exercise unnecessary. Usually it is sufficient to caution agencies that a certain action will make it impossible to certify conformity with the terms of the Social Security Act as a basis for further grants. Often, however, grants have been somewhat delayed to clear up an issue. This practice does not improve federal-state relations, but it is usually effective. Once standards have become settled and state agencies familiar with the policies of the Board, there should be few cases in which this device need be employed, and those requiring actual withdrawal of support should be extremely rare.

## CHAPTER VII

### RESEARCH AND TECHNICAL SERVICE

THE DEVELOPMENT OF the unemployment compensation system has depended to a great extent upon research and technical service. Because it is a new undertaking in the United States and differs in many fundamental respects from the unemployment insurance plans of other countries, it has presented a succession of unexplored problems for state and federal authorities. It has been necessary to formulate new and rather elaborate procedures and record systems, to determine how these procedures should be staffed and mechanized, to estimate the probable volume of benefit claims and the personnel and facilities needed in handling them, and to train a force of many thousands of employees in unemployment compensation operations. Basic decisions of policy and method, which in some cases have had far-reaching effects on the success of the program, have had to be made almost entirely in advance of experience. To illustrate: in one large state a mistake in a single feature of the benefit procedure resulted in the accumulation of more than 350,000 undetermined claims by the end of the first year and caused a practical breakdown of the system. In several states defective wage reporting and recording procedures produced serious delays and inaccuracies in handling tens of thousands of claims during the early months of benefit payment. Experience has strikingly demonstrated that the success or failure of states in the payment of benefits for partial unemployment is largely determined by the methods applied.

#### FEDERAL RESPONSIBILITY FOR RESEARCH AND TECHNICAL SERVICE

In the beginning the states were almost entirely dependent upon the Social Security Board for advice and assistance on technical problems. Most state administrators sought the aid of the Board in planning the organization of their agencies, laying out basic procedures, and dealing with many of the more difficult or fundamental questions with which they were faced. While operating experience has made them much more self-sufficient, technical service is still a very important activity of the Board. Whatever may be the attitude of state unemployment compensation officials toward federal regulation, most are convinced of the need



for a broad federal research program and a competent staff of federal specialists to help the agencies in meeting their problems. In fact, one of the criticisms of the Board has been that it has not been equipped to render as much or as expert assistance as state officials have desired. None of the states has had the staff needed to analyze the numerous questions which have confronted it. After all, the states are primarily the operating agencies of the unemployment compensation system. As a rule, the technical personnel they possess are largely preoccupied with current operations and have little time to devote to the more fundamental or time-consuming problems.

The federal agency can maintain a large technical staff which permits specialization and intensive work on individual problems, whereas no single state can make efficient use of the large corps of specialists that the system as a whole requires. The federal agency also has ready access to the experience of all the states. Furthermore, most of the problems are common to many states, and the solutions discovered often have nationwide significance. The Social Security Board, therefore, has a peculiarly great responsibility for fostering and providing technical service and research. The more adequate they become, the simpler is its task in the supervision of state operations. This assistance to the agencies may properly be viewed as the highest and certainly the most productive type of supervision. Through it more has been done to make unemployment compensation effective than through any other activity conducted by the Board.

### THE FEDERAL TECHNICAL STAFF AND ITS WORK

In organizing its own staff, the Social Security Board was confronted with the same difficulty with which the states were faced in building their agencies—the almost complete lack of persons trained in unemployment compensation. Consequently, it was forced to recruit its technical personnel from other fields which might afford some pertinent experience. Probably the largest group consisted of economists and statisticians, including several with special training in labor problems. A few had been engaged in labor relations or personnel work. Another group was composed of accountants to assist in developing and installing record-keeping and accounting systems. In addition, there was a sprinkling of persons drawn from administration and business management. To develop the background of its staff, the Board conducted during the

first two years an in-service training program for new employees. This program went into subjects such as the philosophy and economics of unemployment compensation, the foreign systems of unemployment insurance, the organization of the Board and the state agencies, and the provisions of the Social Security Act and the Draft Bill.

Technical work in unemployment compensation was originally divided among the Bureau of Unemployment Compensation, the Bureau of Research and Statistics, and the accounting staff of the Bureau of Accounts and Audits, but was eventually concentrated in the first of these agencies, which has since become the Bureau of Employment Security.<sup>1</sup> The Research and Statistics Division of the Bureau of Employment Security carries on the more basic and long-range studies in unemployment compensation and employment service and operates the statistical system, while the Division of Unemployment Compensation deals with the more immediate and applied problems.

The studies of the Research and Statistics Division have covered a variety of aspects of unemployment compensation. In cooperation with some other federal agencies and with the New York Division of Placement and Unemployment Insurance, it has prepared and assisted in installing a standard industrial classification now applied by state agencies in classifying employers. It has also worked out the statistical reporting system used for unemployment compensation and employment service and has helped the states to adjust their procedures to produce the required information. Representatives of the Division working in the field advise state research and statistical personnel on studies being undertaken by the agencies and aid them in planning their projects. To an increasing extent the agencies are carrying on in cooperation with the Division research of more than local significance, particularly studies involving the use of data available only in the states, such as analyses of the effects of various benefit formulas and experience rating schemes.

The staff of the Research and Statistics Division has made special studies of seasonal and partial unemployment, experience rating, and several of the other complex features of unemployment compensation. It has also prepared comprehensive reports on the interpretation of voluntary quitting, discharge for misconduct, refusal of suitable work, and

<sup>1</sup> The State Technical Advisory Service, which specializes in personnel problems, should also be mentioned. Its work has already been described in Chapter VI. Technical service on legislation has been dealt with in Chapter III. The General Counsel's Office also assists state agencies on difficult legal problems and often helps in the preparation of briefs in important cases.

other causes of unemployment which disqualify workers for benefits. Several actuarial studies have been made to determine the effects of changes in benefit formulas, waiting period requirements, etc., and the ability of existing contribution rates to maintain the solvency of state unemployment compensation funds.

The Division of Unemployment Compensation and the technical units which preceded it have done a large part of the more basic developmental work on methods of administering unemployment compensation. As the program has moved from one stage to another, they have analyzed the problems ahead and devised plans for submission to the states. In the beginning this meant the preparation of plans for the organization of new agencies and the inauguration of contribution collection. Next came the formulation of methods for reporting and recording employee earnings, and then the construction of benefit and appeals procedures. Since then, attention has been focused mainly on refinements, simplifications, and means of increasing operating efficiency.

Each stage has involved the drafting of regulations, procedures, and records for the guidance of state agencies. In some cases alternative plans have been prepared and in some but a single scheme. As a rule, only the basic procedural pattern has been suggested and the construction of the detailed procedures for its application has been left to the states or to federal accountants working with the agencies, but some proposals have been issued in detailed form. Especially during the first two years, a large amount of record and procedure planning work was done in the states, mainly by the accountants assisting the agencies in elaborating or revamping procedures and in installing record systems.

The importance of the developmental work performed by the technical staff of the Board, however, should not obscure the contribution of the state agencies to the formulation of unemployment compensation methods. Considerable pioneering was done by a few states before the Bureau of Unemployment Compensation was equipped to render service. Wisconsin in particular, being the first state to adopt unemployment compensation and the first by eighteen months to pay benefits, devised its own plan of operation completely. While the peculiarities of its law made many of its methods inappropriate for other states, its experience was used considerably by the Board and the agencies in planning procedures. New York and New Hampshire also were among the first to begin operation and contributed to the development of procedures for establishing the liability of employers and collecting contributions.

Throughout the developmental period there was a great deal of combining of initial state experience and a constant exchange of ideas on methods between federal and state personnel. It would be impossible, therefore, to determine the extent to which the plans and procedures suggested by the federal agency were actually formulated by its own personnel and the extent to which they originated in the states. In so far as the latter was the case, the Board served as the mechanism for assembling and analyzing new proposals and passing them on to other states. The development of effective methods of operation was a common problem of state and federal staffs, and the plans eventually adopted were the product of joint effort.

Nor should the part played by office equipment companies be overlooked. On account of the large amount of business machinery required, a few leading manufacturers gave intensive study to unemployment compensation and prepared systems of procedure suited to the use of their equipment. Much of the more detailed procedure planning and a large amount of the installation work were done by their representatives. Without this type of service, many of the agencies would have had great difficulty in implementing the more general procedures formulated by the Board or their own personnel, and the federal accounting staff would have been swamped with installation work.

#### EXTENT AND NATURE OF THE SERVICE

The haste with which many state agencies had to begin operation afforded little opportunity for planning, and practically compelled them to obtain their initial blue prints from the Social Security Board. Nearly half the unemployment compensation laws were enacted in the last two months of 1936 and a large part of them provided for the payment of benefits in January 1938. This allowed only a year in which to organize the agency, recruit the staff, lay out the procedures, begin the collection of contributions and wage records, and prepare to handle claims. The task would have been difficult under any circumstances, but it was greatly enlarged by the business recession in the fall of 1937. The unprecedented increase in unemployment in the weeks immediately preceding benefit payment built up an avalanche of claims which descended upon the agencies with terrific force in January 1938. They probably will never again be subjected to so great a work load even in a severe depression.

*The Initial Period*

By the time most of the agencies came into existence, the Board had reached the point where it could be of real assistance to them. Shortly after the wave of legislation had subsided at the end of 1936, the Bureau of Unemployment Compensation issued a report on the organization and staffing of state agencies.<sup>2</sup> This report outlined the activities which an agency would have to perform and indicated the chief organization units it would probably require, as well as the principal positions and types of personnel needed. The Bureau also prepared an outline of the steps an agency must take in launching the collection of contributions, including suggestions on how to discover and determine the liability of employers and set up the initial records. In addition, it drafted regulations and forms suitable for state adoption and developed a considerable collection of materials for the use of new agencies.

Almost the first act of a new state administrator was to come to Washington for a discussion of plans and grants. Most officials undertook their work with little, if any, previous acquaintance with unemployment compensation. Except for a few who were drawn from the field of workmen's compensation, most had had no experience in an enterprise in any way resembling unemployment insurance. In fact, some had had little administrative experience of any kind. The need for advice and assistance was, therefore, great.

On his initial visit to the Social Security Board, the state administrator usually took up his budgetary problems and conferred at length with members of the staff on the first steps to be taken in launching the unemployment compensation program. In some cases the first budget was largely worked out in Washington. During his stay he usually went over the plans for his organization with officers of the Bureau of Unemployment Compensation and discussed staffing requirements with them. With others he canvassed the problems of determining employer liability and beginning the collection of contributions. Before leaving Washington, he received drafts of suggested regulations and forms and a statement of the actions which states had found necessary in the early stages of operation. An examination of the regulations, forms, and procedures adopted by new agencies early in 1937 shows a striking degree of similarity. Many took the federal drafts exactly as they stood; a few even

<sup>2</sup> Social Security Board, Bureau of Unemployment Compensation, *State Unemployment Compensation Agencies, Organization and Personnel*, January 1937.

adopted forms and regulations without stopping to insert the name of the state in the blanks left in the drafts.

After employer lists had been prepared, many of the agencies obtained federal assistance in classifying employers and designing the contribution accounts. States were encouraged to install the standard industrial classification. This usually required the aid of a federal classifier to train an employee of the state agency and start the work. Within a year most of the states had adopted this classification, which now makes possible comparable nation-wide data on employment and payrolls for most industries.

The federal accounting staff was used extensively by new agencies in developing their contribution accounts and in laying out their collection procedures; but this phase of unemployment compensation administration involved fewer unfamiliar problems than any other part of the work. In the main, contribution administration is analogous to other collection operations in government and private business. The major difficulties arose not in formulating records and procedures, but in locating small employers, determining liability in marginal cases, and educating employers in the reporting requirements. In many states contribution administration was on a current basis within a few months.<sup>3</sup>

### *Wage Records and Reporting*

The next step in setting up the unemployment compensation system was the establishment of the wage reporting system. This presented a basic procedural problem. Wisconsin had adopted a plan requiring employers to report workers' earnings only in case of separation from employment. As these data are needed only for persons who become unemployed and claim benefits, this plan, if effective in providing the information promptly and accurately, keeps reporting and record keeping at a minimum. The alternative was the requirement of periodic reports on the earnings of all insured workers and the maintenance of an immense wage record system. This plan had to be used in the administration of old-age insurance because of the manner in which insurance benefits were determined. After much discussion the Social Security Board declared in favor of this scheme for unemployment compensation as well, largely to avoid the danger of delay and incomplete reporting

<sup>3</sup> Contribution administration was complicated in many states by the fact that the payroll levy was made retroactive to the beginning of 1936 in order to take full advantage of the 90 per cent offset against the federal tax. Hence, agencies coming into existence at the beginning of 1937 had to collect two years' contributions during the first year of operation.

inherent in the separation report plan and to enable the agencies to check and control the reports obtained. It was feared that many employers would not maintain adequate payroll records and would be unable to furnish reliable wage data for the full period used in computing benefits. The Board did not make its policy absolutely binding. Nevertheless, only one state other than Wisconsin adopted the separation plan of reporting for all employers, though several allowed its use by limited numbers of concerns with unusually stable employment.

The adoption of periodic wage reporting confronted the agencies with a record-keeping problem of extraordinary proportions. Three general systems were devised for handling it. One was to set up a separate ledger account for each worker to which his earnings were posted, quarter by quarter, from employers' reports. Another was to punch a tabulation card for each worker listed on the quarterly wage reports submitted by employers and to sort and file these cards mechanically by the social security account numbers of the workers. The third plan was to require wages to be reported on a separate slip for each employee and then to sort and file these slips manually by social security numbers. The federal agency did not recommend any one method, though some of its staff originally leaned heavily toward the first in assisting states to set up their systems. Later experience indicated this plan to be cumbersome and inflexible and led the Board to urge its abandonment in favor of the other two. At present these are the standard methods in nearly all states.

### *The Beginning of Benefit Payment*

Benefit procedure presented by far the most difficult technical problems of unemployment compensation administration. In addition, most of the states which started benefit payment at the opening of 1938 were handicapped in developing benefit systems by the fact that their energies had to be concentrated on more immediate tasks. Before they could get their contribution collection machinery operating smoothly and complete their wage records, benefit payment was upon them. Only a few agencies were in a position to devote the time and thought required to work out the benefit problem for themselves. It was essential, therefore, that the Social Security Board assume the responsibility for developing basic plans. Had it not done so, the unemployment compensation system would have foundered sadly in some parts of the country in the first half of 1938.

Early in 1937 the Bureau of Unemployment Compensation set up a

special unit to formulate benefit plans and the following summer issued a memorandum on benefit payment procedures which laid the foundation for the systems later adopted in most of the states.<sup>4</sup> In the preparation of this report, several fundamental issues had to be faced. How frequently should workers be required to report their unemployment—weekly as in Wisconsin, or three times a week as in England? Should they report in person or by mail? Should eligibility for benefits be determined by the local or the central office of the state agency? Should benefits be paid in cash at the local employment office, as in Europe, or by check issued by the central office of the agency? If the latter plan were used, should checks be prepared by the central office only on receipt of pay-orders attesting the claimants' continued unemployment, or should the central office set up a continuing benefit roll and issue checks weekly for each claimant listed thereon until it received a stop-order from the local office? These were the underlying problems in working out the plan of benefit procedure. In attacking them, the Bureau considered European practice to some extent, but drew much more heavily upon the experience of Wisconsin, which had started benefit payment the preceding summer.<sup>5</sup> It is interesting to note that on all but one of these questions the Bureau came to the same conclusion that Wisconsin had reached, and on the one issue the difference was not great.

The procedure suggested by the Bureau provided that the worker would file his claim for benefits and report each week in person at the local employment office which would determine his availability for employment. From his wage record the central office would determine his eligibility in so far as it depended on previous earnings in insured employment, and would compute his benefit rate and duration. A notice of this determination would then be sent to the local office. After the completion of the waiting period, the central office would write a benefit check each week on receipt of a pay-order from the local office establishing the worker's continued eligibility. These checks would be mailed directly to the claimant or be distributed through the local office. In substance, this was the basic plan followed by all but one of the states in beginning the payment of benefits. One state provided for filing claims by mail and substituted a post-card notice for weekly reporting at the

<sup>4</sup> Social Security Board, Bureau of Unemployment Compensation, *Benefit Payment Procedures*, Memorandum I, July 1937.

<sup>5</sup> For a discussion of the Wisconsin benefit system, see Matscheck and Atkinson, *The Administration of Unemployment Compensation Benefits in Wisconsin, July 1, 1936, to June 30, 1937* (Chicago: Public Administration Service, 1937).



local office. It also adopted the stop-order instead of the weekly pay-order method of controlling the issuance of checks. This procedure proved seriously defective and ultimately caused a complete breakdown and reorganization of the agency.

Toward the end of 1937 and the beginning of 1938, the Social Security Board issued a series of memoranda dealing with special phases of benefit procedure and presenting somewhat more detailed methods for handling them. Among these were a procedure for the payment of benefits for partial unemployment, a plan for dealing with mass layoffs, and a procedure for handling appeals. The Bureau also prepared, for the information of the states in handling questions of disqualification and eligibility, a codification of the decisions of the British Umpire in unemployment insurance cases.

The Bureau did not issue benefit procedures elaborated in the detail required for actual operation. Their formulation was left to the state agencies with the aid of the federal accounting staff and of the representatives of the business machine companies supplying the equipment selected by the state. Numerous conferences were held between members of the federal staff, state officials, and machine company representatives during the preparation of the detailed state procedures. Upon completion they were submitted to the Bureau for review. Further conferences were then held on the proposals, and suggestions were offered for their revision. In addition, the Interstate Conference of Unemployment Compensation Agencies held a meeting mainly devoted to benefit problems, and the Bureau conducted a training conference for persons responsible for training state employees in benefit operations.

The closing weeks of 1937 were a hectic period for both state and federal staffs. Besides completing the plans of operation, the agencies had to open hundreds of new employment offices, obtain quarters for the enlargement of their central offices, install equipment, and select and train new personnel several times as numerous as their existing forces. As the year neared the end, it became evident that, due to the business recession, the volume of benefit claims would be vastly greater than had been expected. This necessitated a large, last minute increase in personnel and facilities. Most of the agencies handled these problems for themselves with some technical aid from the Bureau, but a few were so slow in perfecting their organizations that it became necessary to send federal representatives to assist officials in completing arrangements. For example, in one large state the field staff of the United States Employ-

ment Service selected the quarters for many of the employment offices and even negotiated the leases, while persons from the Bureau of Unemployment Compensation helped to complete the procedures and prepare instructions on handling benefit claims.

During the first few months of 1938, the Bureau stationed a special representative in each benefit-paying state to keep in touch with developments and to aid the agency. Some of these representatives rendered yeoman's service in helping agencies to adjust their procedures and cope with their problems, while others were merely observers. For a few weeks the Treasury Department made available a number of its field accountants as special advisers. Though they had little time to acquaint themselves with the peculiarities of the program, several were of very real assistance to the agencies.

In view of the unexpectedly great volume of claims encountered at the outset of benefit operations—more than 2,100,000 initial claims were filed in the first month, most in the first two weeks—it does credit to state officials that they were able to meet the emergency and make unemployment compensation function. Though nearly all the agencies fell a few weeks behind in the payment of benefits in the first quarter of 1938, most succeeded in becoming reasonably current in their operations before the end of the second quarter. Two or three kept abreast of the work from the start, while a few did not catch up until the following year.

### *Simplification of Benefit Procedures*

A few weeks of benefit payment demonstrated the necessity of simplifying procedures to permit more rapid operation. Some of the difficulties arose from defects in the methods originally adopted, and some from complications in the laws themselves. Many were attributable to over-refinements either of law or of procedure. The benefit formula contained in the Draft Bill and copied with variations by most of the states was too intricate for workers to understand or the agencies to apply in a large-scale operation. Some of the procedures also were needlessly elaborate. To cite an extreme case, one state required local offices to prepare eight typewritten copies of each claim which were routed to various central and local units. Nearly all agencies set up file folders for each claimant in both local and central offices. The files expanded so rapidly that space could scarcely be found in which to store the records. A small claim record card, developed by the Bureau and the Virginia

agency, in itself has produced a great simplification of local office work and eliminated hundreds of filing cabinets. Multiple-purpose records and packs of forms have also been devised which have greatly reduced paper work and speeded up operations. This streamlining process has been a joint effort of the federal and state agencies. The Bureau, however, has taken the leadership in developing simplifications in the benefit formula and other features of the unemployment compensation laws.<sup>6</sup>

Those states which did not begin benefit payment until 1939 were able to profit by the experience of the others and to avoid most of the difficulties they had encountered. Furthermore, the claims loads were much lighter than in January 1938. To a far greater degree the agencies starting payment in 1939 were able to plan their own procedures and handle their tasks unaided, though they obtained from regional representatives and others much valuable counsel based on the work of the previous year.

### *Installation of Experience Rating*

The last major step in the installation of unemployment compensation has been the establishment of experience rating systems. While the federal agency has devised plans for the maintenance of employer experience rating accounts and has assisted some states in shaping their procedures, the agencies have prepared their own plans to a greater extent than in the earlier phases of the unemployment compensation program. This has been due both to delay on the part of the Board in analyzing experience rating and to the increased experience of the agencies in formulating procedures. It indicates greater maturity and self-sufficiency on the part of the agencies. This, in turn, points to a decline in federal influence and to the necessity of greater expertness in dealing with technical problems if the federal agency is to render effective service in the field of operating methods.

## DEFICIENCIES OF FEDERAL TECHNICAL SERVICE

Important as the federal contribution has been to the development of unemployment compensation, the technical service of the Social Security Board has seldom equalled the needs of the state agencies. Frequently, the plans and procedures which it has formulated have been too

<sup>6</sup> Social Security Board, Bureau of Unemployment Compensation, *Simplification of the Benefit Formula in State Unemployment Compensation Laws*, February 1939.

long delayed. In some cases, as with the memoranda on handling mass layoffs and the payment of benefits for partial unemployment, its suggestions have not reached the states until after they have had to start operation. In fact, only one of a series of twelve reports on benefit procedures was issued before the beginning of benefit payment, though many of the ideas contained in these studies were discussed with state officials and incorporated in the procedures of many of the states before the publication of the reports themselves. Similarly, the report on the simplification of the benefit formula in state laws was not released until March 1939, though action was desired during the legislative sessions of that year.<sup>7</sup> With experience rating also, many of the states had to develop procedures and begin operation before the Bureau was able to render much assistance.

The delay in supplying technical aids has been due to several causes. The most important have been the limited size of the federal staff and the large number of problems to be dealt with in the early stages of the program. The division of control over operations among fifty-one independent agencies has greatly added to the time required for conferences, review of state proposals, and service to the agencies, and has often prevented the Bureau from attacking problems as promptly as desirable. The board form of organization at the federal level has also retarded action at times, though it has probably resulted in more carefully considered recommendations.

In the study of technical problems and the development of new methods, the federal staff has been handicapped by remoteness from the scene of operation. During the first few years most of the technical work in the field was done by the accountants who assisted states in detailing and installing their procedures. The persons engaged in research and the more basic planning were tied down in Washington for the most part, with little opportunity to observe unemployment compensation in actual operation. It was, therefore, hard for them to visualize some of the problems assigned them and to appraise the operating difficulties which often vitally affect the practicability of proposals. To overcome this handicap, the technical personnel now spend a considerable part of their time in the field.

<sup>7</sup> The report did not reach the states until the middle of March. Drafts of amendments covering many of the suggestions were issued in January 1939, but they were not accompanied by the explanation and analysis needed to aid state officials in developing legislative proposals.

## MEANS OF STRENGTHENING FEDERAL TECHNICAL SERVICE

While unemployment compensation has now passed the early planning stage, there is still a great need for research and technical service in perfecting its operation. Undoubtedly much more can now be done to increase efficiency and reduce costs through aid in solving technical problems and in improving operating methods than by minute review of budgets and detailed supervision of state administration. Lengthening the budgetary period and reconstructing the accounting systems to yield expenditure data susceptible of comparative cost analysis should reduce the federal personnel required for fiscal work and permit an expansion of the technical staff. An increase in the latter force should hasten improvements in the administration of unemployment compensation and result in savings in grants equal to several times the expenditure for the additional federal personnel.

The states, however, are no longer novices in dealing with unemployment compensation problems. Many of them have developed competent technicians within their own staffs, and all have a fund of practical experience which is basic in perfecting the unemployment compensation system. But they lack breadth of perspective and ability to specialize. Their research and technical people have to cover the entire unemployment compensation program and frequently must carry some administrative responsibilities as well. The aid they particularly need from the federal staff is that of the specialist who has studied one aspect of the program intensively and is familiar with the way in which it is handled in other states.<sup>8</sup> It is easy for the personnel of an agency to get into a rut and to become provincial in their thinking. Yet there is a keen interest among them in the practices of other states and a desire to learn from national studies and the work of other agencies.

The development of a corps of technical experts is one of the most important tasks of the Bureau of Employment Security, but this takes time. The day has passed when the personnel can be properly trained in Washington. Unemployment compensation is now a program in action, and the states are the laboratories where it must be studied. Since the rush of preparing the agencies for benefit payment has subsided, the Bureau

<sup>8</sup> When asked by the author to indicate the most helpful services obtained from the Board, state officials have commonly referred to work done in the agency by persons particularly expert on a certain phase of the work. As between specialized and generalized service, they have invariably indicated the need for more of the former.

has to a much greater degree been assigning individuals to particular subjects and sending them into the states to analyze specific aspects of the program and to absorb in detail the problems and the methods used. An intensive program of field studies is essential to obtain the background needed to aid the states and to command their respect, but to a large degree these studies can be combined with service to the agencies after the preliminary work has been done.

One means of hastening the analysis of unemployment compensation problems would be the temporary use of state personnel on national projects. Scattered among the agencies are many persons of special competence who have a knowledge of actual operations such as few of the federal staff possess. While they could not be permanently withdrawn without injury to their agencies, most could be spared for a few months to assist the Bureau on surveys or special studies or to render technical service in other states. In this way the Bureau could obtain additional staff with which to press forward its own research and technical programs. The federal agency would benefit from the operating experience of the state personnel, and the states, from the broadened backgrounds acquired by members of their staffs and the new ideas and information they would bring back to their agencies. The arrangement would also help to break down some of the barriers between state and federal agencies and to create closer working relations between them.

The solution of state problems could also be hastened by greater provision for the clearance of ideas and experience among agencies. Very few of the problems are peculiar to any one state. Most have arisen and been met in different ways and with varying degrees of success in a number of states. Yet state officials usually are acquainted only with the plans tried by their own agencies and perhaps a few adjoining states. With this limited background, it often happens that one agency is considering the adoption of measures which have already been tested and perhaps discarded by another. There have even been cases in which one state has proposed a basic change of system, such as the substitution of tabulating for bookkeeping equipment, while another nearby state has been considering the opposite change for reasons believed by its officials to be equally compelling.

As a rule, the Bureau does not publish a report until it has been able to examine a problem minutely and arrive at definite recommendations. But long before this the agencies have to take action, often on the basis

of very limited analysis. A greater interchange of ideas in advance of final conclusions would often be helpful. This need might be met in part through the *Employment Security Review*, the periodical published by the Bureau. Articles explaining problems and methods in individual states would provide a clearance of experience which would be of value to both state and federal personnel. A similar result could be obtained by greater use of regional and sectional conferences of state administrative and technical personnel. Annual conferences are now held in most regions under the auspices of the Interstate Conference of Unemployment Compensation Agencies, but these meetings are too brief and too infrequent to permit a thorough discussion of the many problems now confronting agencies. They could, however, be developed into very valuable professional gatherings.

The Bureau has already made some use of the survey technique to improve state administration and develop its own personnel. With increased staff, much more use could profitably be made of this device. Many defects in operation go unnoticed because of the limited acquaintance of state and regional personnel with alternative methods. Substantial savings could often be made by improvements of organization and procedure which a competent survey staff should be able to suggest. This has been amply demonstrated in the few states where comprehensive surveys have been made.<sup>9</sup> There probably are few agencies that would not benefit by a thorough examination of their systems by an outside group well grounded in the various features of unemployment compensation administration.

While most of the specialization must take place in the central staff of the Bureau, good, all-round technical personnel in the regions is also essential. Every region could utilize the services of at least one person particularly familiar with unemployment compensation problems and procedures, and another possessing a similar knowledge of employment service. The regional representative, as a rule, is preoccupied with budgetary and administrative problems and does not have the time or the training for thorough analysis of state operating methods. Consequently, defects may not be observed unless they definitely obstruct operation. It is noteworthy that the Bureau of Employment Security receives more requests for technical advice and assistance from regions where there is

<sup>9</sup> One of the early surveys led to simplifications which produced a reduction of more than \$100,000 in the next budget.

a well-equipped technical person on the regional staff than from other areas. Not only can he detect conditions which call for improvement, but on many he can render the service needed by the agency. In other cases he provides a valuable connecting link between the agency and the specialized staff of the Bureau.



## CHAPTER VIII

# COORDINATION OF SOCIAL INSURANCE AGENCIES AND SYSTEMS

THE ADMINISTRATION of social insurance in the United States presents a tangled web with many gaps and numerous overlapping strands. Workmen's compensation, the oldest form of social insurance in this country, is entirely administered by the states. Though unemployment compensation constitutes a federal-state system, its administration is divided among fifty-three state and federal agencies. In addition, there is a separate unemployment insurance system for railroad employees, operated by the Railroad Retirement Board. If unemployment compensation is extended to maritime workers, another federal system will no doubt be established for that group. Finally, there are two old-age insurance systems—one for workers generally and the other for railroad employees—administered through three separate federal agencies.<sup>1</sup>

The existence of fifty-three state or federal laws and fifty-four state or federal agencies for the administration of unemployment insurance inevitably calls for the closest possible coordination. This chapter will consider some of the major problems of coordination,<sup>2</sup> but cannot attempt to cover the entire field, for the issues are numerous and many need further exploration.

### EMPLOYER COVERAGE

While the provisions of unemployment compensation laws on employer coverage conform for the most part to the basic pattern of the Draft Bill, there are sufficient variations in definitions and exclusions to add to the difficulties of state administrators and of employers operating in more than one state. An interstate employer must acquaint himself with the unemployment compensation laws, regulations, and interpretations of the states in which he does business or run the risk of subjecting

<sup>1</sup> The numbers used in this paragraph take into account the tax administration and fund management functions performed by the Treasury Department for the various social insurance systems.

<sup>2</sup> For a discussion of another group of coordination problems, see C. A. Kulp, *Social Insurance Coordination* (Washington: Committee on Social Security of the Social Science Research Council, 1938), pp. 271-306.

himself to penalties and perhaps impairing the benefit rights of his workers. Several elaborate commercial services and a growing literature have come into existence to aid employers in threading their way through this new field of law.

### *Interstate Employment*

The physical division of the country into fifty-one state and territorial jurisdictions for the administration of unemployment compensation inevitably creates many coverage problems. If the operations of an interstate employer are confined to separate plants located in different states and each establishment maintains its own payroll, the determination of coverage does not ordinarily present particular difficulty. But if a group of salesmen for a Philadelphia concern operate from a branch office in Kansas City, Missouri, and cover Oklahoma, Kansas, and Nebraska, it becomes more complex. Similarly, problems are apt to arise when a building contractor operating in New York, Connecticut, and New Jersey shifts his force from one state to another. Likewise, if an Illinois trucking company has drivers in Cleveland for a regular run to New York City, there may be questions. In the case of a large corporation, situations like these and perhaps several other types may exist. If differences in laws and interpretations are added, it is evident that the determination of coverage has its perplexities for employers and state officials. The manner in which these and other coverage problems are resolved affects not only the reporting burden of the employer, but also the convenience with which employees obtain benefits when unemployed and sometimes their ability to qualify for benefits. Owing to differences of law, some employment may escape coverage entirely, while some may technically be liable to taxation in more than one state.

To a great degree, gaps and duplication in the coverage of interstate employment have been eliminated by amendments worked out by the Social Security Board and the Interstate Conference of Unemployment Compensation Agencies late in 1936 and since incorporated in the laws of most states.<sup>3</sup> In brief, these amendments provide that employment shall be deemed localized and subject to coverage in a particular state if entirely performed therein or if the service without the state is incidental to that performed within it. If the employment does not fall in either of these categories but is partially performed in one state, it is to be cov-

<sup>3</sup> Social Security Board, *Draft Bills for State Unemployment Compensation of Pooled Fund and Employer Reserve Account Types*, revised edition, January 1937, sec. 2(i).

ered there, provided the base of operations or point of control is in that state. In case the base of operations or point of control is not in any state in which work is performed, the employment is to be covered in the state where the worker resides. Finally, should none of these conditions be fulfilled, the employment may be covered in the state where the worker resides. Though these provisions are somewhat complicated and often difficult to apply, they take account of most of the interstate situations which arise. A few states, however, have not yet adopted them, or have added them to other provisions with which they are not entirely consistent.

One of the important problems which the existing coverage provisions do not adequately meet is that of the contractor who shifts his operations and his force from state to state. If the base of operations moves, presumably the state of coverage likewise changes. But it is not always clear whether the contractor has actually shifted his headquarters. He may have moved his office to the new project, but with the intention of returning to the former state on completion of the work. Even if it is apparent that the base of operations has changed and that the employment is covered in the new state, the force may have been recruited and may reside in the former state. In this case, it would be better for the workers to have their benefit rights accumulate in that state, so that there would be no loss of benefits due to the division of their employment among several states. As yet no satisfactory solution has been developed for this type of situation. In so far as the workers are concerned, it could be met by a plan for the transfer of benefit rights, which will be discussed at a later point in this chapter, but this would not remove the difficulties for the employer and the state agencies.

### *Exclusions from Coverage*

State laws differ more in their exclusions from coverage than in the provisions relating to interstate employment. The major difference is in the size of establishment exempted. In eleven states, coverage extends to employers having but a single worker, as it does in the federal old-age and survivors insurance system, while in twenty-five, it applies only to those having eight or more employees. Industrial exclusions vary in minor respects, but are tending to conform to those of the Federal Unemployment Tax Act. Differences in exclusions do not create administrative problems of importance, but they result in inequitable treatment of workers and employers, both among states and in the individual states.

One bricklayer employed by a large concern is covered by unemployment compensation, while another working for a small contractor in the same community is not. Similarly, an employer with ten employees is subject to the payroll tax, while a competitor next door with seven workers escapes. Yet another across the state line may be liable though he has only five employees.

A revision of coverage provisions to afford broader and more uniform protection to workers in the various states would be desirable. Inasmuch as the old-age and survivors insurance system has demonstrated the feasibility of covering small employers, it would seem that unemployment compensation might well be extended to their workers. The inclusion of small employers creates operating difficulties, but several states have shown that they can be met with reasonable success. Moreover, these problems are partially offset by others—such as the subcontractor problem—which are largely eliminated by taking in small employers. The accomplishment of a broader and more uniform coverage hinges mainly on the amendment of the Federal Unemployment Tax Act. If the definition of employment in the federal Act were broadened, the states would soon revise their laws to conform, since the 90 per cent offset provision would leave little reason for failing to give workers the protection of unemployment compensation.

#### *Railroad Unemployment Insurance Coverage*

The establishment of a separate system of unemployment insurance for railroad workers has created a new group of coverage problems. In addition to the carriers themselves, the Railroad Unemployment Insurance Act applies to any company, directly or indirectly owned or controlled by carriers, which “operates any equipment or facility or performs any service (except trucking service, casual service, and the casual operation of equipment or facilities) in connection with the transportation of passengers or property by railroad,” together with railway labor organizations and certain railroad bureaus and associations such as traffic associations.<sup>4</sup> Many companies serving carriers, but not themselves engaged in the transportation of passengers or freight, have been held to come within the provisions of the Act. For example, refrigeration companies which ice railroad cars, and the Fred Harvey Company, which operates station restaurants and dining car services on certain lines, have been held to be covered by the Act. A few electric railways and some

<sup>4</sup> 52 Stat. L. 1094.

motor bus companies operating partly in connection with steam railways are also considered subject to the Railroad Unemployment Insurance Act.

These concerns, together with carloading companies, terminal warehouse companies, and a few other groups, form a twilight zone between the railroad unemployment insurance and the state unemployment compensation systems. Several of the basic issues of coverage have not yet been definitely decided. Some of the companies are covered by the Railroad Unemployment Insurance Act for part of their employment and by state unemployment compensation laws for the remainder. Often the same employees are engaged in both types of work in the course of a year.

Obviously, dual coverage greatly complicates an employer's problem, for he must keep the two classes of employment separate in his payroll records and comply with the reporting requirements of two very different insurance systems. The number of companies which fall in this twilight zone is small, but the number of employees affected is considerable. As with interstate workers, those employed by concerns subject to both state and railroad unemployment insurance systems may have divided benefit rights, which for some may mean the loss, and for others the enlargement, of benefits. It may be possible to eliminate some of these difficulties by amendment of the Railroad Unemployment Insurance Act to exclude certain marginal groups of employers entirely and leave them subject only to state unemployment compensation laws. Some of the problems, however, are inherent in the existence of separate insurance systems and can be removed only by consolidation.

### COLLECTION OF PAYROLL TAXES

Fifty-three agencies are engaged in the administration of fifty-five separate payroll taxes for unemployment or old-age insurance purposes.<sup>5</sup> Two of these agencies and four of the taxes are federal and the rest are state or territorial. The Bureau of Internal Revenue administers the payroll taxes for old-age and survivors insurance and for railroad retirement, as well as the federal unemployment tax, while the Railroad Retirement Board collects the tax for railroad unemployment insurance. The federal unemployment tax and in large measure the tax for old-age

<sup>5</sup> This includes the fifty-one state employment security agencies, the Bureau of Internal Revenue, and the Railroad Retirement Board. In addition to the fifty-five payroll taxes, there are taxes on employees' wages for old-age and survivors insurance and for railroad retirement.

and survivors insurance involve the same employers as the state unemployment compensation levies. Except for very small employers, most are subject to three payroll taxes, two collected by the Bureau of Internal Revenue and the other by the state unemployment compensation agency. Besides this, large numbers of employers are paying unemployment compensation contributions in more than one state, some in nearly all states.

The multiplicity of agencies administering payroll taxes and the overlapping of federal and state taxes cause a great amount of wasteful duplication of effort for employers and the government. Employers must prepare three sets of tax returns for most of their employment. These returns are different in form, and—what is more important—the definitions of the employment subject to tax are also somewhat different.<sup>6</sup> In administering the taxes, the Bureau of Internal Revenue and the state agencies have almost identical tasks to perform. They must discover and establish the liability of employers subject to the tax, collect and account for the revenue, follow up delinquents, and examine employers' records to detect evasion and determine the accuracy of the returns.

### *National Administration of Contributions*

The obvious duplication of work involved in the present system of payroll taxes has led many to urge national administration of the payroll levies for unemployment compensation. If this change were adopted, it would be possible to combine the three payroll taxes on a single return and to collect them all at the same time. One agency, presumably the Bureau of Internal Revenue, would determine employer liability under each tax, handle the collection, and audit employers' accounts. The adoption of this plan would probably be accompanied by revisions of the federal acts to provide identical coverage for the unemployment compensation and the old-age and survivors insurance taxes. Employers, however, would probably have to report the distribution of their payrolls by state of coverage, as they now do for the federal unemployment tax. From these data the Bureau of Internal Revenue could then compute the amount due each state as its share of the unemployment compensation levy and make a periodic settlement with each.<sup>7</sup>

<sup>6</sup> The 1939 amendments to the Social Security Act made the definitions of employment practically uniform for the two federal payroll taxes levied by the Act, except that the tax for old-age and survivors insurance applies to employers having one or more workers and the unemployment tax only to those with eight or more.

<sup>7</sup> Other methods of apportionment could be used, but this seems the logical plan with a federal-state system for the administration of unemployment compensation.

Unified national administration of the payroll taxes would be a considerable simplification for employers. They could deal with one taxing agency and would have but a single set of coverage provisions to observe and one return to prepare. Much of the confusion involved in the present arrangement would be eliminated.<sup>8</sup> At the same time, unified administration would eliminate costly duplication of effort between the Bureau of Internal Revenue and the state agencies. It would no longer be necessary for both to operate collection systems or to audit employers' records to determine the accuracy of their tax returns.

National administration of unemployment compensation contributions, however, presents problems and difficulties which greatly limit its practicability and possible savings so long as other unemployment compensation operations are carried on by state agencies under separate state laws. First of all, it would be necessary to obtain uniform coverage provisions in all the states. This probably would not be particularly difficult to achieve, assuming that the coverage of the federal unemployment tax were enlarged to coincide with that of the tax for old-age and survivors insurance, as convenience of administration would demand. The states would then quickly adjust their laws to conform. In the second place, the necessity of distributing the proceeds of the tax to the state where the employment occurred would force interstate employers to make the same difficult allocation of their payrolls as at present and would continue to raise questions of the situs of coverage for the agency administering the tax.

A third problem would be that of keeping the states informed of the amount of payroll reported by each employer, period by period, as a basis for verifying their employee wage records. One of the principal advantages of the present system of periodic wage reporting is that it permits the agency to compare the sum of the wages shown on the employee wage reports filed by an employer with the payroll total shown on his contribution report. As the latter is subject to verification by field audit, this comparison serves as a means of checking the completeness and accuracy of the wage reports from which benefits are computed. But this need could be satisfied by having the Bureau of Internal Revenue furnish each state a list of the employers paying taxes on employment therein, with the payroll amount. Or it could be met more easily by re-

<sup>8</sup> Many small employers have not understood the distinction between state and federal payroll taxes and have assumed that the payment of one or the other satisfied all the requirements of the social security system.

quiring employers to submit their tax returns in duplicate and then sending one copy to the state in which the employment was covered. As a basis for the maintenance of experience rating accounts, it would also be necessary to furnish states with experience rating systems a record of the amount of unemployment compensation contributions paid by each employer.

The real obstacle to national collection of unemployment compensation contributions is individual employer experience rating. Forty states now provide for some form of experience rating by which the contribution rate of each employer is annually determined with reference to some supposed measure of his unemployment risk. The most usual scheme is the so-called charge-back system. Under this plan a separate account is maintained for each employer, to which are credited the contributions paid by him. Against this account are charged the benefits paid to his former employees in accordance with rules laid down by the state law. The excess of contributions over benefit charges during a stipulated period is termed the reserve balance. Each year the state agency computes the ratio of this reserve balance to the employer's average annual payroll for a three- or five-year period, as provided in the law, and, by applying a scale contained in the law, fixes his new contribution rate according to the percentage which his reserve balance is of his average annual payroll amount. Thus, a 10 per cent reserve ratio may entitle the employer to a one per cent contribution rate. These scales and some other features of the scheme differ from state to state.

To comply with the requirements of the charge-back system of experience rating, which is substantially the one prescribed by most state unemployment compensation laws, the following steps would be necessary with national administration of unemployment compensation payroll levies:

- (1) Upon receipt of the tax payments, the Bureau of Internal Revenue would have to total the payments creditable to each state and notify it of the amount of unemployment compensation contributions paid by each employer on employment covered therein. For the purpose of verifying the wage records maintained by the state, the Bureau would also have to inform it of the total amount of payroll shown on each employer's tax return for each period.

- (2) The state agency would have to maintain a separate ledger account for each employer, to which it would credit his contribution payments and charge the benefits paid to his employees.



(3) The state agency would annually have to compute the new contribution rate for each employer and transmit a statement of the new rates to the Bureau of Internal Revenue in advance of the first collection for the new year.

(4) The Bureau of Internal Revenue would have to enter the individual rates determined by the state agencies for the various employers on the tax blanks mailed to them, or in some other manner notify them of their new rates. For an employer operating in more than one state, there would usually be a different rate for each state.

This analysis indicates that national administration would make little, if any, difference in the amount of contribution accounting required in state agencies and would greatly increase the amount of information to be cleared between the states and the Bureau of Internal Revenue. It would also make the administration of payroll taxes much more costly and cumbersome for the Bureau. Moreover, it would not entirely eliminate overlapping between the states and the Bureau in the investigation of employers for the determination of employer liability. A large percentage of the new employers added to coverage—probably a majority in states which cover employers with one or more employees—are brought to light by benefit claims filed by workers. If a claimant reported employment not indicated by state wage records, it would often be necessary for the agency to investigate in order to determine whether the employer was subject to the unemployment compensation law. Hence, the states would continue to require field forces and to discover new employers who should be paying unemployment compensation contributions. A similar situation now exists in the administration of old-age and survivors insurance and the payroll tax for its support. The Social Security Board operates the insurance system and handles the benefit claims, while the Bureau of Internal Revenue administers the tax. Though both are federal agencies, the arrangement has proved sufficiently cumbersome and has given rise to enough difficulties of coordination to cause some to wonder whether the administration of both the tax and the benefits should not be vested in a single agency.

From the standpoint of employers, unified national administration of the payroll taxes would represent a material simplification. But so long as state laws provide for individual employer experience rating, it is by no means clear that national administration would involve enough reduction of work or expense for governmental agencies to compensate for the increased intergovernmental clearances and for the division of re-

sponsibility for the determination of coverage between the state benefit-paying agencies and the federal tax-collecting agency. While some state officials have expressed themselves as favoring national administration of unemployment compensation contributions, there is no certainty that an attempt to bring about this change might not meet almost as much political opposition as would a move to nationalize the entire system. In fact, nationalization of the tax would be a considerable step toward federal administration of unemployment compensation.

It is not meant by this discussion to deny that unified administration of the payroll taxes in itself has many advantages, but rather to indicate that, considered in conjunction with other features of the existing federal-state system of unemployment compensation, the advantages are much less compelling than is often believed. If experience rating were abandoned throughout the country, unified tax administration would be much more feasible and might well prove the best arrangement.

#### *Coordination of Existing Systems of Tax Administration*

For the present, better coordination between state and federal agencies probably affords a more practicable means of improving the administration of payroll taxes than an attempt to nationalize the collection of unemployment compensation contributions. It is patently absurd for state agencies and the Bureau of Internal Revenue independently to be ferreting out little employers and collecting payroll taxes without more constructive cooperation between them than now exists. Particularly is this true where the state unemployment compensation law applies to employers with one or more workers, as does the federal tax for old-age and survivors insurance. The mortality among little employers is great; they come and go by the tens and hundreds of thousands. Many keep only the crudest records and are ignorant of their obligations under the social security system. At best, the application of payroll taxes to small employers is difficult, and the percentage who escape detection is bound to be substantial. Both the Bureau of Internal Revenue and the state agencies need all the aid the other can give if they are to enforce these taxes effectively against the little employer. It is not that the loss of revenue is so material; at times it costs more to collect the tax than it yields. Instead, it is the effect of inadequate tax enforcement on the benefit rights of workers which is important. Unless employers are discovered and made to comply with the tax and reporting requirements of

the state and federal laws, workers are likely to suffer loss either in unemployment compensation or in old-age benefits.

At present, the cooperation between the Bureau of Internal Revenue and the state agencies is rather limited. The only formal clearance of information is an annual certification by the states of the amount of contributions paid by each employer having eight or more workers. This is essential in the application of the 90 per cent offset against the federal unemployment tax and provides a very valuable aid to the Bureau in the administration of that tax. On the other hand, the states are not provided with a regular clearance of information from the Bureau. The data on employers subject to the tax for old-age and survivors insurance, which would be of great value to states covering employers with less than eight employees, are held to be confidential information which can be obtained by state officials only on formal application by the governor and then by a rather cumbersome process. Clearly, the federal act should be amended to make this information more readily available to the state agencies.

In enforcing payroll taxes, the Bureau of Internal Revenue and a state agency each enjoys advantages which the other lacks and which account for numerous returns. On its side, the Bureau of Internal Revenue has the advantage of the prestige of the federal government and the information in its income tax files. With little effort on its part, the Bureau obtains returns from thousands of small employers who do not wish to run the risk of federal penalties, but who stand in little awe of their state government. On their side, the state agencies have the advantages of large forces of field investigators—aggregating more than half the number employed by the Bureau of Internal Revenue for the enforcement of all federal taxes—and of the benefit claims filed by unemployed workers. These claims have proved to be the most productive means of discovering non-complying employers in states with a very low coverage. Between one-sixth and one-quarter of the insured workers file unemployment compensation claims in the course of a year and have an opportunity to report inaccuracies in their wage records. If the record is incomplete and a worker objects, the agency investigates. This means that the state agencies have several million enforcement agents for the unemployment compensation system to help discover employers who should be, but are not, reporting and paying their taxes, or who are not filing complete returns. The Bureau of Internal Revenue has no enforcement device of equal

strength. Obviously, there should be simple, routine procedures for the clearance of information between the state and federal agencies so that both may the better and the more easily fulfill their responsibilities under the social security laws.

In states having a very low coverage limit, and especially in those covering employers with one or more workers, there could be a useful two-way clearance between the state and federal agencies on new employers and on those going out of business. The mechanics of clearance could be rather simple. Probably there should be an initial comparison of employers' lists, which the state agencies could make by checking copies of the federal list against their files of active employers. Thereafter, the state agencies could meet the needs of the Bureau of Internal Revenue by merely furnishing a carbon copy of the liability and status reports filed by new employers, and by periodically sending the Bureau a list of employers whose liability had terminated—prepared by running the address plates removed from the active file. From the liability and status report, the Bureau could usually determine whether the employer was subject to the federal tax and, if liable and not paying, could notify him by mail to show cause why he should not file a federal return. Although the Bureau could not give the state agencies a comparable record, it could readily produce from its address plates lists of newly liable employers which would show the names and addresses of the firms and the number of insured workers. On termination of liability, it could give the state a similar list. This procedure would involve relatively little work for either agency and would promptly bring to the attention of each the new employers discovered by the other, and the concerns quitting business whose records should be checked at once for delinquent taxes.

There could also be a valuable clearance of field audit and investigation reports which have revealed additional tax liability. It is reasonable to suppose that the employer who, through ignorance or intent, has filed an incomplete return with one agency has likewise submitted an inaccurate report to the other. Many of the states use standard forms to summarize audits and investigations of employers' records, and the preparation of a carbon copy for the Bureau of Internal Revenue would be sufficient. In return the Bureau could notify the states by letter of the findings of its field investigators, but legislation might be necessary to make the information available. That such an interchange of information would be very productive, there can be no doubt. In one large state alone, field audits made in 1939 revealed over \$3,000,000 of un-

reported liability for unemployment compensation contributions. In most states with which the author is acquainted, the field audit forces have produced revenue far in excess of their cost.

Interstate cooperation in the audit or investigation of out-of-state employers presents a type of coordination which has already been developed to some extent by the state agencies. Often the payroll records of an interstate employer are centralized at a single office, and a considerable saving is possible by having the agency in that state conduct the audit for all the states concerned. A certain interstate comity has also developed in making other types of field contacts and investigations. The principal difficulty arises from the differences in state laws and interpretations and the possibility that the field man may fail to conform to the law of the foreign state for which he is rendering service.

#### WAGE REPORTING

Wage reporting offers another fruitful field for coordination. Both unemployment compensation and the benefits paid by the old-age and survivors insurance system are based on the previous earnings of the individual worker. Consequently, both the state agencies administering unemployment compensation and the Bureau of Old-Age and Survivors Insurance of the Social Security Board maintain elaborate wage record systems. In the case of unemployment compensation, these records only extend over a one- or two-year period, but in old-age and survivors insurance they accumulate for the earning lifetime of the worker. To supply the necessary data, employers must file with the federal government a quarterly report of the earnings of all their insured employees and in nearly all states either a quarterly or an annual report of the wages of all those covered by unemployment compensation. For all workers earning \$1,000 or more a year, they must also file an annual wage report with the Bureau of Internal Revenue for income tax purposes.

Thus, employers must submit three different wage reports for their workers, and in some states a fourth report to the state income tax authority. That this multiple reporting is costly as well as irksome to employers is obvious. It is also apparent that the maintenance of duplicate systems of wage records is expensive for state and federal social insurance agencies.

One suggestion for overcoming multiple reporting is that there should be a single system of wage records and reporting for unemployment

compensation and old-age and survivors insurance, operated by the latter. The Social Security Board maintains an immense central record office for old-age and survivors insurance. If the coverage for unemployment compensation were made uniform with that for old-age and survivors insurance, one set of wage reports and records could supply the information required for both. But so long as one insurance system is operated by the federal government and the other by the states, there appears to be little possibility of consolidating the wage records. The Social Security Board at one time considered breaking up its wage records among the twelve regional offices, but, after careful study, found that this would be much more costly and less convenient than a centralized record system. The annual saving by centralization has been estimated at \$700,000.<sup>9</sup>

It is very unlikely that a single national record office could furnish wage information to state agencies with sufficient promptness for the determination and payment of unemployment compensation claims. In fact, there may be question whether twelve regional offices could supply the necessary data quickly enough, though it is possible that they might. The procedure would be slower than under a complete regional system of unemployment compensation administration, since transactions would flow from the local to the central office of the state agency, then to the regional office and back to the central office in the state, rather than directly from the local to the regional office. To make a single wage record system function efficiently, the administration of unemployment compensation would have to be entirely nationalized.

Even with a dual system of wage records for social insurance purposes, much could be done to lighten the reporting burden for employers and to reduce administrative costs. If the states would adopt uniform definitions of employment and wages in conformity with those in the federal social security laws, it would be possible to use a standard form of wage report which would enable employers to prepare the reports for unemployment compensation and old-age and survivors insurance at one operation, one as a carbon copy of the other. The main obstacle to this plan is that the federal government has found a list type of report preferable for its purposes, whereas the procedures employed in many of the state agencies necessitate obtaining the data for each worker on a separate wage slip. The Social Security Board originally used the slip type

<sup>9</sup> Social Security Board, *Fourth Annual Report*, 1939, p. 19.

of report. While wage slips are a little less convenient for the Bureau of Internal Revenue and the Bureau of Old-Age and Survivors Insurance, both of which handle the reports, the difference would hardly be great enough to justify compelling employers to prepare the reports separately. It would be much easier for the Board to shift to wage slips in states where the unemployment compensation procedure requires them, than for the states to change their record systems and business equipment to make efficient use of the list type of report.<sup>10</sup> If this were done, a uniform wage report could be used within each state for unemployment compensation and old-age and survivors insurance, and employers would gain the principal advantages of an integrated system of wage reporting.

With some changes in the benefit formulas prescribed by state unemployment compensation laws and by the Social Security Act for old-age and survivors insurance, there could be a great reduction in the volume of wage-reporting and record-keeping work for both employers and the agencies. A few states base all benefit computations on the worker's earnings in the preceding calendar year and determine the weekly benefit rate from his wages in the quarter of highest earnings during that year. With this plan it is possible to allow employers having reliable and properly protected payroll records to file annual, rather than quarterly, wage reports, provided they break the data down into quarterly amounts. One state adopting this plan has placed nearly half its employers on an annual reporting basis. As most of the large employers maintain good records, annual reporting applies to three-fourths of the workers in the state. This represents an immense reduction in reporting for employers and in record keeping for the agency. With annual reporting, the wage slip plan is definitely the most economical for unemployment compensation purposes.

If the benefit formula for old-age and survivors insurance were slightly revised, it would also be possible for the Social Security Board to adopt annual wage reporting for employers with proper payroll records. Not only would this reduce reporting for the employers, but it would mean a great cut in record-posting work for the Bureau of Old-Age and

<sup>10</sup> With list reports, the state must punch a tabulation card for each wage entry and use tabulating machinery for its benefit operations. With the slip system, the slips are sorted and filed manually, and bookkeeping equipment is used for benefit operations. As yet, the relative efficiency of the two plans has not definitely been determined, and there would not be an adequate case for asking states to abandon slip reporting. In fact, it may well be that it is the preferable system for unemployment compensation.

Survivors Insurance. With the use of the slip type of report, it would also be possible to devise a standard form which could be prepared in sufficient copies to meet the wage-reporting needs of unemployment compensation, old-age and survivors insurance, and the Bureau of Internal Revenue. It would be desirable, in addition, to require the employer to give a copy of the wage slip to the worker, if still in his employ, so that the worker could request its revision if inaccurate. This requirement would be a good enforcement device and would bring about a prompt correction of many of the errors and omissions in wage reports.<sup>11</sup>

In view of the opportunity for employers and governmental agencies to save labor and expense, serious study might well be given to a plan of wage reporting such as that outlined above. While it would involve some changes in benefit formulas, they would not lessen the adequacy of benefits. In so far as unemployment compensation is concerned, they are changes which have already been effected in a number of states and have proved satisfactory.

#### CLEARANCE OF WAGE RECORD CORRECTIONS

With the dual system of wage records for unemployment compensation and old-age and survivors insurance, there could be an exchange of correction data. At best, hundreds of thousands of errors are bound to creep into the records in the course of a year, many inconsequential, but some sufficient to have a material effect on benefit calculations. Though a source of delay and annoyance, these errors are less serious for unemployment compensation than for old-age and survivors insurance, because only the most recent year's earnings are used and the worker can usually detect the inaccuracies if substantial. Each year hundreds of thousands of workers do contest the accuracy of their unemployment compensation determinations. The agencies then obtain the worker's account of his employment and earnings during the period on which benefits are based and re-examine their records to discover errors. If necessary, they get in touch with the employers to obtain revised wage reports. In this manner large numbers of employee earnings records are corrected each year and new benefit determinations issued. It is estimated that in 1939 approximately 5,000,000 of the 27,500,000 workers

<sup>11</sup> If the worker did not care to take the matter up with his employer, he could file a complaint at the employment office and the agency could institute an investigation.



covered by unemployment compensation filed benefit claims. Consequently, about 18 per cent of the insured workers had an opportunity to pass upon the accuracy of their wage records and to protest if they believed the records inaccurate. Since these were the workers with unstable employment, it is reasonable to presume that they represented a high percentage, quite possibly a majority, of the serious errors and omissions in the wage records.

The Bureau of Old-Age and Survivors Insurance has no comparable means of discovering errors and obtaining the correction of its wage records. If an employer fails to report for a given worker or enters an incorrect wage amount, the Bureau cannot detect the mistake, provided the sum of the amounts reported for all his employees agrees mathematically with the total on the wage list report and with the total payroll shown on his tax return for the same period. As the unemployment compensation and old-age and survivors insurance wage reports are prepared from the same records, it is probable that the major errors or omissions will appear in both. It should, therefore, be very advantageous to the old-age and survivors insurance system to obtain from the states the corrections made in unemployment compensation wage records as a result of benefit claims, and thus eliminate a large proportion of the errors which it will be too late to remedy when the worker files his claim at the age of sixty-five.

The exact form of clearance would have to be worked out with reference to the records and procedures used by the individual state agency. All states with periodic wage reporting prepare a transcript of the wage data in some form as a basis for each new benefit determination. Many send a copy to the local office to be shown to the worker. If he contests its accuracy and errors are discovered, either the old transcript is corrected or a revised transcript is prepared. A copy of the revised transcript with the changes indicated would provide the information needed by the Bureau of Old-Age and Survivors Insurance to correct its records. It would seem that a routine procedure might readily be devised for supplying these data to the Bureau. This clearance would be especially valuable with states covering employers with one or more workers. In states with higher coverage limits, a substantial proportion of the unemployment compensation corrections would consist of wage data obtained from newly discovered employers along the margin of the coverage limit who might have been reporting for old-age and survivors insur-

ance. Nevertheless, the percentage of other types of corrections might be sufficient to render the clearance worth while.<sup>12</sup>

### PAYMENT OF BENEFITS TO MULTI-STATE WORKERS

The interstate worker presents especially difficult problems in the operation of the federal-state system of unemployment compensation. As benefits are based on the past earnings and employment which are reported to the state where the employment is localized, state boundaries have an important effect upon a worker's ability to obtain compensation. Two general types of situations may be noted. In the first, the unemployed worker resides in one state but has had his employment, and hence his benefit rights, in another. This group of workers may again be divided into two classes: the regular commuters living only a short distance from the state of their employment and normally expecting to obtain their future employment in that state, and the persons who reside at a considerable distance from the state where their benefit rights have accrued, such as construction workers who have been employed on a distant project, or young factory employees who, after losing their jobs, have returned to live with their parents in other states.

The second type of situation arises when the worker has had employment in two or more states, as is often the case with construction workers and some other groups. This type presents the more difficult problems. At one extreme, the division of employment may mean that the worker cannot qualify for benefits in any state, and at the other, he may be able to draw benefits from two or more states greatly in excess of the amount he could secure in any one of them if his employment had been confined to that state. Also, it may be possible for him to draw benefits from two states simultaneously, though this would usually be contrary to the unemployment compensation laws and regulations.

To meet the problem of the interstate worker, at least in part, the Inter-

<sup>12</sup> A few experiments have been conducted in the clearance of employee wage data from the Bureau of Old-Age and Survivors Insurance to the states. For example, New York has obtained wage data from the federal agency on some of its unemployment compensation cases which have been appealed because of incorrect wage records. In nearly half the cases the Bureau was able to supply part, and in more than one-fourth of the cases all, of the needed information. In New England there has been an experiment in furnishing states correction data obtained by the Bureau of Internal Revenue after a preliminary scrutiny of the wage reports filed with it preliminary to transmission to the Bureau of Old-Age and Survivors Insurance. Most of these corrections involved failure of the employer to report his workers' social security account numbers. The states make a similar examination of their wage reports and routinely write employers for the missing information.

state Conference of Unemployment Compensation Agencies, with the aid of the Social Security Board, has prepared a plan for the payment of benefits to these persons which has been adopted by practically all the agencies. Under this plan an employment office in one state will accept the claim of a worker who has had his employment in another state and transmit it to the central office of the latter state. This central office then determines the claim in accordance with its state law and its wage records, and sends the determination to the local office which took the claim. The worker is required to report to the employment office weekly in the usual manner. It takes and transmits continued claims evidencing the worker's continued unemployment and eligibility for benefits. After the waiting period has been served, as provided by the law of the state against which the claim was filed, the central office begins the payment of benefits by check addressed to the claimant.

This procedure operates reasonably well if the claimant has had all of his employment in one state and does not shift from place to place after filing his claim, as some migratory workers do. It is somewhat slower and more cumbersome, of course, than the regular procedure for intra-state claims, and it places a greater burden on the local and central office staffs handling the claims, as they must familiarize themselves with the requirements and methods of many states. The plan only provides for the payment of benefits for total unemployment, but in practice many, though a minority, of the states also accept interstate claims for partial unemployment benefits.

The principal deficiency of the scheme is its failure to make proper provision for the payment of benefits to persons with insured employment in more than one state. To qualify for benefits in any state, the claimant must have had sufficient earnings in that state to establish his eligibility in the same manner as though he had done all his work there. In many states minimum earnings of from \$150 to \$200 during the base year are necessary to qualify for benefits. Consequently, the worker who has been employed in several states may forfeit part of the benefits to which he would otherwise have been entitled because he has not had sufficient earnings in some of these states to establish his eligibility. In some cases, earnings are so scattered that the worker can obtain no benefits at all or only a small fraction of what he would have obtained had his employment been concentrated in one place. On the other hand, an occasional claimant has had sufficient earnings in each of two states to entitle him to the maximum amount of benefits allowed by law in each,

and thus may draw benefits for twice the period normally permitted. Another difficulty in the operation of the plan when the claimant has benefit rights in two or more states is that many of them require a complete waiting period to be served after they receive the claim. As no claim is transmitted to state B until the worker has exhausted his benefit rights with state A, this involves serving two waiting periods, whereas only one would normally be required.

The problems presented by interstate workers are not insoluble, though the solutions would involve some operating difficulties and require amendment of the unemployment compensation laws of many states. Methods already in use appear to be as well adapted as any to certain of the situations that have to be met. A threefold plan would seem reasonably adequate to take care of the principal situations that arise. For commuters residing in one state and having all their insured employment in an adjoining state, the best arrangement would appear to be to require the claimant to file his claim and report at the nearest local office in the state of employment, provided the commuting cost is not excessive. This allows the transaction to be handled like an intrastate claim. For the worker who has had all his employment in one state but cannot reasonably be required to file his claim and report there owing to the distance or the travel cost, the present multi-state procedure is appropriate, although it ought to be extended to provide for partial as well as total unemployment. In this case, the worker would file his claim with the employment office nearest his residence, and it would be forwarded to the central office in the state where the benefit rights had been accrued.

For workers who have had insured employment in more than one state, yet a third arrangement is needed. Various schemes have been proposed, but probably as practical a plan as any would be for the state where the worker is located to accept and pay the claim in accordance with its own unemployment compensation law, and subsequently distribute the cost and bill the other states in which the claimant had worked during the base period. Under this scheme the worker would file his claim with the nearest employment office, which would obtain a list of the states in which he had worked during the base period provided by its own law and the approximate dates of the employment. It would then transmit the claim to its central office. The central office would request the other states where the claimant had worked to forward transcripts of his wage records. After assembling this information, it would combine the wage data and determine the claim in accordance with the bene-

fit formula provided by its own law. The worker would report at the nearest local office each week as required by the rules. On completion of the regular waiting period, the central office would pay benefits in the usual manner and up to the same limits as if it were handling an intrastate claim.

After the exhaustion of benefits or upon the completion of the benefit year, the agency handling the claim would apportion the benefit payments among the various states in which the claimant had worked, according to the ratio of benefits to earnings provided by its own law, and would charge the other states in the inverse chronological order in which the employment occurred. The states would periodically bill each other for the benefits paid or clear the transactions through the federal Bureau of Employment Security, as provided in an agreement among the agencies.

A plan of this kind for dealing with workers having employment in more than one state would overcome most of the difficulties in the present procedure. It would avoid loss of benefits due to earnings being scattered among a number of states and would also prevent the payment of excessive amounts of benefits to workers having sufficient earnings to qualify for maximum benefits in more than one state under the present procedure. Furthermore, it would eliminate the necessity of serving more than one waiting period in a benefit year and would allow the claims to be handled substantially in accordance with the normal procedure for intrastate claims. There would, of course, be some problems to be unsnarled. One of the principal difficulties would be that of obtaining wage data for the proper period from states which take the calendar year as the base period and use annual wage reporting. Special provisions would also have to be adopted for Wisconsin and any other states which have unusual benefit formulas or which base the duration of benefits on the number of weeks of employment rather than on the amount of earnings.

The establishment of a separate unemployment insurance system for railroad employees has created benefit problems similar to those arising with interstate workers. In fact, the problems are somewhat more difficult because the benefit features of the railroad unemployment insurance system differ more from those of the unemployment compensation system than the state laws differ among themselves. The Railroad Unemployment Insurance Act bases benefits on days of unemployment rather than on loss of earnings during a seven-day period. Whereas most states

compute the claimant's weekly benefit rate from his wages during the quarter of highest earnings in the preceding year, the daily benefit rate for railroad unemployment insurance is determined from annual earnings. These and other differences in the two systems have importance because many railroad workers have non-railroad employment in the course of a year. Particularly is this true of maintenance-of-way employees, whose railroad employment is definitely seasonal.

Some study is being given to the possibility of combining railroad and state benefit rights for claimants with both railroad and non-railroad employment and having one agency pay the benefits for both insurance systems. The Railroad Unemployment Insurance Act would permit the Railroad Retirement Board to enter into agreements with state agencies for this purpose and to reimburse them for benefits paid on earnings derived from railroad employment. The plan would follow somewhat the lines indicated above for persons who have worked in two or more states, but would require special provisions to take care of the fundamental differences in the two insurance systems.

## CHAPTER IX

### MAINTENANCE OF AN ADEQUATE BENEFIT STRUCTURE

THE FUTURE OF UNEMPLOYMENT COMPENSATION laws largely rests with rival employer and employee interest groups in the states. The leadership in legislation, originally exercised by the Social Security Board, is rapidly passing, not to state employment security agencies familiar with unemployment compensation problems, but to private organizations. In many states employer groups are aggressively seeking reductions in contribution rates and a restriction of benefits, and in a few they have already forced the enactment of such amendments. Though much less articulate and informed, organized labor is beginning to demand increased benefits. Either of these pressures, if not subject to restraint, could seriously endanger the unemployment compensation system—employer pressure by so reducing contributions as to lead to ultimate insolvency or by so limiting benefits as to impair the value of unemployment compensation, and employee pressure by so raising the benefit scale as eventually to bankrupt the system.

#### ADDITIONAL NATIONAL STANDARDS

This condition raises the question whether additional standards should be inserted in the Social Security Act with reference to the benefit and contribution provisions of state laws in order to assure the accomplishment of the purposes of the federal Act.

#### *Reasons for Additional Standards*

One of the principal reasons for urging the enactment of additional federal standards is the need of establishing a benefit structure more nearly adequate to tide insured workers over their periods of involuntary unemployment. The benefit provisions of the early Draft Bill did not represent what the President's Committee on Economic Security and the Social Security Board deemed an adequate system of unemployment compensation. Rather, these provisions represented a very conservative estimate of what they believed a 3 per cent payroll tax would finance

over the span of a business cycle.<sup>1</sup> Twenty-six weeks within a year—as in Great Britain—were considered the most desirable maximum duration of unemployment benefits; but sixteen weeks were thought to be the longest period for which benefits could be provided with a 3 per cent tax, which seemed the highest practicable levy. In the light of existing information, it is now believed that the 3 per cent tax would have permitted a longer benefit duration than the authors of the program thought possible from the fragmentary data on which they had to base their estimates.

A few principles afford a reasonable basis for determining what constitutes an adequate benefit structure. In the first place, the benefit rate should be at least sufficient, as a rule, to enable the unemployed worker to maintain his family in health and decency without supplementary relief.<sup>2</sup> Second, the payment of benefits should begin early enough to avoid hardship and the necessity of seeking public assistance. Finally, the duration of benefits should be sufficiently long to carry the vast majority, certainly 80 per cent or more, of the normally employed workers through the unemployment they experience within a year, except in prolonged periods of depression.<sup>3</sup> Unless unemployment compensation can meet these tests, it will require considerable supplementation by other forms of public assistance and will fall short of its objective of maintaining the regular working force without resorting to relief in case of any except the more extraordinary unemployment hazards.<sup>4</sup>

Two and a half years of benefit payment experience have demonstrated that the existing benefit structure does not meet these tests. A large percentage—in some states a majority—of the insured workers exhaust their benefit rights before they are able to return to work. Sample studies in 1938 and 1939 indicated that in Michigan 48 per cent of the claimants exhausted their benefits; in Iowa, 75 per cent; and in New

<sup>1</sup> See Arthur J. Altmeyer, "Liberalizing Unemployment Compensation," *Social Security Bulletin*, January 1940, pp. 1-3.

<sup>2</sup> It is recognized that the regular benefit rate cannot be sufficient to provide for some unusually large families or for extraordinary expenses due to illness in the home. These cases inevitably require special treatment.

<sup>3</sup> Unemployment due to disability or the worker's refusal of suitable work is excluded, of course, from unemployment compensation.

<sup>4</sup> Paul L. Stanchfield has defined adequate benefits as follows: "Benefit payments at a weekly rate comparing favorably with the relief grant or WPA wage which the claimant would receive if in need, continued for a long enough period to cover all unemployment (except the waiting period) experienced by the great majority of eligible claimants during the benefit year." (Social Security Board, Bureau of Employment Security, *Unemployment Compensation Contributions, Benefits and Reserves* [Employment Security Memorandum No. 5, 1940], p. 24)



Hampshire, 55 per cent. For these workers the duration of unemployment compensation was obviously too short. In some states the weekly benefit rate also is too low. In North Carolina 70 per cent of the benefit payments for total unemployment amount to less than \$6 per week. In one other state the average weekly benefit payment is less than \$6, and in five more, between \$6 and \$7. Especially in large cities, relief agencies have found it necessary to supplement unemployment benefits in many cases. For low-paid workers a benefit rate of one-half the regular wage is not sufficient to maintain the family in health and decency, though in general, the benefit rate is less open to criticism than the duration of benefits. For many workers the two- and three-week waiting period requirements have also proved a hardship. With a two-week waiting period, the worker must be unemployed for three weeks before he is entitled to a week of benefits and an additional week must usually elapse before the check arrives.

But national standards are needed, not merely to obtain a more adequate benefit structure, but to protect the existing one from being weakened by the insistent demand of employer groups for reduced contributions. In most states experience rating permits a reduction in an employer's contribution rate if his contributions over a period of years exceed by a certain margin the amount charged against his account for benefits paid to his employees. Though the purpose is to stimulate efforts to stabilize employment, it is really a decrease in benefit charges rather than more stable employment that reduces an employer's contribution rate. This decrease can be achieved as well by restrictive amendments to the unemployment compensation law as by an actual reduction in unemployment; in many states and for many industries it can, no doubt, be obtained much more easily by amendment. The fact must be plainly recognized, therefore, that experience rating provides a constant incentive for employers to seek benefit reductions by amendment. The better acquainted employers become with the unemployment compensation system, the stronger will be their interest in legislation for this purpose.<sup>5</sup>

The danger is by no means imaginary. In many states labor is no match for the employer group before the legislature. Throughout the South and in the predominantly agricultural states, labor as a rule lacks

<sup>5</sup> Before experience rating became operative, employers were not particularly aware of its possibilities and significance. Hence, they were not alert to the desirability of blocking liberalizing amendments or obtaining restrictive legislation. The turning point did not come in many states until after the 1939 session.

effective organization and leadership. On a problem as complex as the revision of benefit formulas or experience rating provisions, it is at a great disadvantage in seeking to protect its interests. Several states have already passed seriously restrictive amendments, and agitation is arising for similar legislation in many more. In 1939 West Virginia amended its benefit formula in a manner which reduced the average benefit rate for total unemployment from \$10.89 to \$7.98. Similar benefit formulas were adopted by Maine, North Carolina, and South Dakota in 1939 and by Kentucky in 1940. The reduction in the average benefit rates of these states since the change ranges from 12 to 27 per cent.<sup>6</sup> The same plan is being urged in a number of other states.<sup>7</sup>

Under similar pressure several states have adopted experience rating plans which permit only reductions in contribution rates. A better-than-average unemployment experience produces a rate reduction, but a worse-than-average experience brings no corresponding increase in the employer's contribution rate above the normal rate of 2.7 per cent. Consequently, the aggregate revenue of the unemployment compensation fund inevitably falls below the yield of the 2.7 per cent tax on which the unemployment compensation system is based. These one-sided experience rating plans run the risk of ultimately exhausting the reserve fund and depressing benefits.

One scheme of experience rating, called the replenishment plan, is particularly apt to bankrupt an unemployment compensation fund at the beginning of a depression. Under this scheme the basic contribution rate in each year is fixed at a point which would raise an amount equal to that expended for benefits in the previous year provided the total amount of employers' payrolls remains the same. This means that in a year such as 1930, when claims and benefit payments would have risen by leaps and bounds, the basic contribution rate would have been one which, if levied on the prosperity payrolls of 1929, would have financed the relatively modest benefits paid in that year. But with the sharp slump in payrolls in 1930, this rate would have produced revenue far less than

<sup>6</sup> Thomas C. Fichandler, "The Effects of Relating Weekly Benefit Amounts to Annual Earnings," *Social Security Bulletin*, April 1940, pp. 7, 8.

<sup>7</sup> A further example of the drive for the restriction of benefits is found in proposals for more stringent eligibility and disqualification provisions. In addition to the usual penalty of an increased waiting period when the worker has voluntarily quit his job or been discharged for misconduct, some states have amended their laws to make a corresponding reduction in his benefit duration for the current year. One state now cancels all benefit rights when a worker goes into self-employment or a woman quits to get married, though either may soon return to covered employment and have later need to draw upon these rights.

the amount of benefits paid in 1929. Thus, the reserve fund would have shrunk rapidly at both ends—through abnormally heavy benefit payments and extraordinarily small contribution collections. This plan also ignores the need for accumulating strong reserves in the good years to tide over the bad ones. This case is cited merely to indicate the danger of amendments which may jeopardize the effectiveness of the unemployment compensation system in the very years when it is most needed.

Another argument for additional national standards is to maintain a reasonable degree of uniformity in the treatment of workers and employers in different states. Since 1938 the trend in state legislation has definitely been toward diversity in contribution and benefit provisions. For example, the maximum amount of benefits a worker may receive within a year now ranges from one-sixth of his earnings in the previous year in some states to one-third in some others; in a few states the only limit is a multiple of the weekly benefit rate, which varies from a low of thirteen to a high of sixteen. A comparison of benefit rates in industrial states of similar character also indicates substantial inequalities. The median rate in the first half of 1940 was \$14.66 in Illinois, \$12.39 in Michigan, \$11.26 in Pennsylvania, \$10.75 in Ohio, and \$10.71 in Wisconsin. Partial unemployment benefits are usually paid by the week, but one state now pays them in part by the month and another only by the quarter.

Whereas contribution rates were a flat 2.7 per cent of payrolls until 1940, existing experience rating schemes permit very substantial differences among states in the average level of contribution rates.<sup>8</sup> With the same degree of unemployment, two employers in the same industry but in different states may have entirely dissimilar contribution rates because of the way in which experience rating is applied. Inequities are bound to arise owing to these variations in the treatment of competitors. The federal unemployment tax and the 90 per cent offset were intended to overcome these inequalities of tax burden and to prevent competition among states in cutting benefit standards and reducing contribution rates. But in the absence of national benefit and contribution standards, experience rating nullifies the purpose of the federal tax. An employer whose state contribution is reduced to zero by experience rating can still obtain the 90 per cent credit against his federal tax under the terms of the Federal Unemployment Tax Act.<sup>9</sup> As the sole requirement on experience

<sup>8</sup> Rate adjustment began in Wisconsin in 1939, but in no other state until 1940.

<sup>9</sup> Section 1602.

rating imposed by federal law is that rate adjustments shall be made only after three years of some sort of "experience bearing a direct relation to unemployment risk," the door is open for a wide variety of experience rating schemes, some of which might deplete reserve funds<sup>10</sup> and give employers a competitive advantage over those of other states. More definite standards in the federal law would help to prevent the adoption of unsound experience rating schemes detrimental to the unemployment compensation system and inequitable in their effects on employers.<sup>11</sup>

If a national reinsurance plan is ultimately established to supplement the weaker state unemployment compensation funds, as seems essential, it will be necessary to write into the federal law a body of standards on benefits and contribution rates. Otherwise, the reinsurance fund might soon be drained away by changes in state unemployment compensation laws. This problem will be further discussed at a later point in this chapter.

### *Objections to Additional Standards*

Several important objections may be raised against the enactment of national standards on contributions and benefits at this early stage in the development of unemployment compensation. In the first place, they run counter to the doctrine of states' rights and the basic philosophy of a state-controlled system of unemployment compensation. This objection, however, should not carry too much weight. After all, the present unemployment compensation system is a federal-state rather than a state system and had its origin in federal legislation. Moreover, one of the major purposes of national standards is to free states of competitive disadvantages due to unequal state levies for unemployment compensation

<sup>10</sup> The Social Security Board has elaborated this provision somewhat by interpretation, but it remains an inadequate protection against ill-conceived experience rating schemes. See Social Security Board, *Standards for the Interpretation of Section 1602(a)(1) of the Internal Revenue Code*, Employment Security Memorandum No. 9, July 1940.

<sup>11</sup> This statement of the dangers inherent in unrestricted experience rating does not indicate that the author is opposed to experience rating as such. He believes that only an actual test can determine whether it will produce a significant and wholesome tendency to stabilize employment. He recognizes, however, that the term "experience rating" embraces a variety of schemes for the adjustment of contribution rates, some of which are based on such crude and unreliable measures of unemployment and are applied in such unscientific ways that they are bound to have very erratic effects on employers' contribution rates. Schemes such as these can scarcely be expected to produce socially desirable results. If experience rating is to be safely used and fairly tested, it must be so designed as to provide a definite incentive for bona fide employment stabilization and to protect the solvency of the unemployment compensation system. This indicates the need for carefully drawn national standards rather than the abandonment of experience rating itself.

and thus to enable them to maintain a socially worth-while plan of insurance.

A more important objection is that national standards limit state experimentation and may, therefore, impede the development of unemployment compensation. The desirability of considerable experimentation in the beginning of the program is obvious. Unemployment compensation cannot yet be crystallized in a rigid, lasting form. To attempt to do so would be shortsighted and unrealistic. While much has been learned from a few years of experience, many problems are not yet sufficiently understood to warrant final conclusions. Existing benefit formulas have not been developed from the analysis of ample data on the amount and the fluctuations of workers' earnings or on the relation of wage rates to living standards. There is no assurance that any of the benefit rate formulas now used represents the best long-run method of calculating benefits. Similarly, there is not yet enough information on the duration of unemployment among the normally employed to indicate the proper point at which to set the limit of benefit duration. The value of experience rating has not yet been demonstrated by actual test, nor have the effects of the various plans of experience rating become known. In fact, the rate of payroll tax necessary to finance the present or any given benefit structure throughout the business cycle is still uncertain and will probably remain so for several years.

Under the circumstances it might seem best to defer the enactment of benefit and contribution standards until there is greater understanding of unemployment compensation problems. Were it not for the possible effects of experience rating and the need of making unemployment compensation a more effective instrument for dealing with the unemployment problem, this might be the appropriate course. But as it is, such standards are needed. All things considered, it would seem wise to protect and, within the limits of the existing financial resources of the system, to improve the level of insurance benefits by inserting suitable provisions in the federal law, and to proceed from that point by amendment as experience indicates the desirability of change. In drafting national requirements at this time, however, considerable latitude should be permitted for variations among the states.

### *Subject Matter of National Standards*

In enacting federal standards to protect the unemployment compensation system so that it may more adequately fulfill its purpose, considera-

tion might well be given to the benefit structure, the level of contributions, and the elements of experience rating.<sup>12</sup>

*Benefit rates.*—Without establishing a uniform benefit rate formula for the country as a whole, it is feasible to draft a federal provision which would afford the needed protection and yet allow considerable flexibility. This can be achieved by setting a basic standard and permitting equivalents. As nearly all states fix the benefit rate as either a percentage of the worker's full-time weekly wage or a fraction of his highest quarter's earnings in a preceding year, these constitute an appropriate basis for a national standard. For example, the requirement might be set up that benefit rates should be related to past earnings and that, on the average and in a majority of cases, the benefit formula should produce a rate not less than 60 per cent of the claimant's most recent full-time weekly wage or one-twentieth of his highest quarter's earnings during a four-quarter period within the nine quarters preceding the filing of his claim.<sup>13</sup> A provision of this kind would fit existing practice in most states and protect a reasonable level of benefits. At the same time, it would leave the way clear for the use of any other type of formula with benefits based on earnings which would, on the average and for most claimants, result in at least as adequate benefit payments. Whether a given formula met the federal standard could be determined statistically from a sample group of claims.

With this standard, a national provision on minimum benefit rates would not be essential but might be worth while. The payment of trivial benefits, frequently requiring relief supplementation, is administratively wasteful and socially ineffective. Usually a rate of about \$5 has been suggested as a national minimum. A flat amount, however, has widely varying significance in different parts of the country. A fair minimum in New York would be excessive in Mississippi, and a limit suitable in the South might be meaningless in some northern states. A possible solution would be to take as the minimum for each state a stipu-

<sup>12</sup> Since this chapter was written, a committee of state employment security officials has issued a very illuminating report on experience rating and the desirability of national standards relating to the benefit structure. The majority report of the committee recommends national standards on most of the subjects covered in the following discussion. See *Report of the Committee on Employer Experience Rating of the Interstate Conference of Employment Security Agencies*, vol. II, pp. 14-25.

<sup>13</sup> Sixty per cent and one-twentieth are used here only for illustration. A higher ratio may be desirable in the lowest earnings brackets. The rule as stated would also permit a lower ratio in the highest earnings brackets. A maximum limit on benefit rates is, of course, necessary. In most states the maximum benefit rate is now \$15 per week.

lated percentage (say 60 per cent) of the median benefit rate paid in the state for total unemployment in the preceding year, subject to outside limits of perhaps \$4 and \$7.50.

*Benefit duration.*—Vital as the duration of benefits is to workers, a reasonably adequate national minimum standard cannot be fixed so long as benefit payments in each state are financed solely from the state's contribution collections. In the absence of reinsurance, a national provision on benefit duration would have to be drawn with reference to the financial capacity of the weakest state unemployment compensation fund.<sup>14</sup> This is a serious deficiency in the present system and a strong reason for some plan of reinsurance.

*Partial benefits.*—There are still four states which do not pay benefits for partial unemployment, and one which does provide them has a quarterly payment plan which largely nullifies the purpose of the compensation. Since, over a period of time, partial unemployment often causes as severe a loss of earnings as total unemployment, no compensation system can be considered complete unless it covers this risk. The Social Security Act might well require the payment of benefits for partial unemployment in a sum at least equal to the amount by which the worker's earnings fall below his benefit rate for total unemployment, plus an allowance of two or three dollars to make partial employment more remunerative than benefits for total unemployment. Partial benefits should be payable not less often than semi-monthly. Monthly or quarterly payment defers benefits too long and also allows much unemployment to go uncompensated.<sup>15</sup>

*Waiting period.*—To be eligible for benefits, a worker must have served a waiting period and have had earnings of at least a given amount during the preceding year. A number of states still require a waiting period of three weeks before benefits begin to accrue, a provision which imposes considerable hardship in many cases. Originally, a substantial waiting period was thought necessary to enable the agency to handle claims, but it is now evident that one week should be sufficient for this

<sup>14</sup> The only other means of financing a reasonable standard of benefit duration would be by forcing the states with weak funds to raise their contribution rates above 2.7 per cent to whatever point might be necessary. This probably would not be feasible.

<sup>15</sup> For a discussion of the effects of quarterly payment in West Virginia and of monthly payment in Michigan, see J. J. Joseph, *An Exploratory Memorandum on Partial Unemployment Benefits in State Unemployment Compensation Systems* (Washington: Committee on Social Security of the Social Science Research Council, Pamphlet No. 4, May 1940), Chapters I, II, IV.

purpose. Though the waiting period is of secondary importance, a uniform national provision of one, or at most two, weeks would have value.

*Eligibility.*—The principal function of a national standard on eligibility would be to prevent a denial of benefits to low-paid workers through the establishment of unduly high eligibility earnings requirements. One state now excludes from benefits all persons who earned less than \$300 in insured employment during the previous year. Another state, located in a low-earnings area, has a requirement of \$200, which excludes large numbers of the most needy workers. To suit the varying wage levels of the country, a national requirement on eligibility could best be fixed as an amount of earnings equal to a stipulated multiple of the claimant's benefit rate, since it reflects his scale of earnings.

*Contributions and experience rating.*—The development of adequate national standards on contributions and experience rating is essential to the future effectiveness of the unemployment compensation system in many states. Probably the simplest method of preventing experience rating from adversely affecting the solvency of unemployment compensation funds would be a national requirement that the rating plan be so designed as to yield revenue substantially equal to 2.7 per cent of the aggregate taxable payrolls in the state. This would permit the adjustment of the rates of individual employers upward or downward according to the relative stability or instability of their employment as determined by any of several measures.<sup>16</sup>

The principal objection to a provision of this kind is that a few states with unusually stable employment might not need an average revenue equal to 2.7 per cent of total payrolls to finance a desirable benefit structure. The District of Columbia is the outstanding example. To avoid the accumulation of excessive reserves, a reduction of the basic rate below 2.7 per cent might be permitted upon (1) compliance with adequate benefit standards and (2) the accumulation of a reserve fund of a certain size. For example, if twenty or twenty-four weeks were found to be a

<sup>16</sup> For fairness to all parties, careful study should be given the type of employment stability and the measures of stability to be used. Several states have taken as the measure of employers' unemployment experience the amount of wages paid by them during a twelve-month period (the base period) to workers who drew some amount of benefits within a period from three to eighteen months subsequent thereto. It would be difficult to show that these particular wage payments provide a logical basis for any given change in an employer's contribution rate. They do not measure the volume of unemployment in his establishment, or the amount of benefits drawn by his former workers, or the instability or irregularity of their employment. Under this scheme a concern would pay a heavier tax if it had a three-week shut-down than it would if it suspended operations for six months and discharged its entire labor force.



sound and desirable limit upon the duration of benefits, then a state meeting other federal standards and providing benefits up to this limit would be entitled to reduce the contribution level below 2.7 per cent when its fund exceeded the stipulated amount.

For the purposes of a national provision, the fund balance upon which a reduction in the basic contribution rate would be contingent probably should be fixed in relation either to the state's annual expenditures for benefits or its annual contribution collections, or both, over a period of years. One plan would be to multiply by two or three (1) the largest amount of contributions collected and (2) the greatest amount of benefits paid for any year within a stipulated period, and then to take the higher of these products as the size of reserve balance which would entitle the state to lower its basic contribution rate. A provision of this kind would have the merits of assuring an adequate benefit structure, providing a reasonably safe but not excessive reserve fund, and at the same time permitting the adjustment of each employer's contribution rate according to the relative stability or instability of his employment. It would afford the protection the unemployment compensation system needs and also provide a direct financial incentive for employers to stabilize their employment.

### REINSURANCE

States differ greatly in the strength of their unemployment compensation funds and in their ability to finance a satisfactory benefit structure. In 1938, when unemployment reached a relatively high point in many areas, the ratio of benefit payments to contribution collections in the twenty-three states paying benefits throughout the year ranged from a low of 26 per cent in the District of Columbia to a high of 143 per cent in Maine. Taken as a group, these states increased their reserves during the year, but in seven the funds declined. Had it not been for the fact that most of these states began payment of benefits before workers had had an opportunity to build up their benefit rights to a normal level, a larger number of states would have shown decreases in their unemployment compensation funds and the reductions would have been far greater in amount. In 1939, when the claims load was much lighter than in 1938, only one state showed an actual decrease in its fund, but the ratio of benefit payments to contribution collections was seven times as great in the state with the heaviest drain on its reserves as in the one with the

lightest. If a sufficient duration of benefits had been provided, the funds would have decreased in a number of states.

### *Necessity of Reinsurance*

The comparative strength or weakness of unemployment compensation funds depends upon differences among states in their benefit scales and experience rating plans and in the nature of their underlying economic systems. Other things being equal, a state such as Michigan, where the automobile industry with its highly seasonal operations provides the bulk of the insured employment, inevitably has heavy demands on its unemployment compensation fund. West Virginia, with its soft coal industry, likewise experiences severe unemployment each year. A scale of benefits which would be economically sound in most states would bankrupt the unemployment compensation system in these states. On the other hand, the District of Columbia, because of the extraordinary stability of its employment, could provide an unusually generous scale of benefits and yet maintain lower contribution rates than other jurisdictions. Studies made by the Social Security Board indicate that in most states the funds apparently could support a longer duration of benefits than the unemployment compensation laws now provide, but in some an extension of benefit duration would be financially impossible.

How a serious depression following a period of normal business activity would affect the unemployment compensation system can only be surmised. It is reasonable to expect the system to become insolvent in a number of states in which mining and heavy manufacturing predominate. States in which trade and light manufacturing provide most of the employment should fare much better. But the unknowns in unemployment compensation are great. There are too many examples of once stable industries which have declined, and of formerly prosperous areas that have run into the doldrums, to warrant the assumption that the unemployment compensation fund of any given state which pays reasonably sufficient benefits will remain solvent over a considerable period of years. States which weather one depression satisfactorily may be less fortunate in another.

If the solvency of the unemployment compensation system is to be maintained in all parts of the country so that workers may obtain the benefits to which they are entitled by law in times of their greatest need, national provision will have to be made for spreading the risk and supplementing the funds of the states which encounter the greatest unem-

ployment. Either there will have to be an outright federal subsidy, or some plan will have to be adopted for pooling risks and building up a national reserve to meet unusual demands upon the system in any area. In private insurance this problem has been met by reinsurance, under which one company shifts part of its risk to others to protect itself against extraordinary or unforeseen hazards. Since its inception, students of unemployment compensation have recognized the need for applying the reinsurance principle to the unemployment compensation system in order to obtain a broader distribution of the risk and preserve the solvency of state funds.

### *Essential National Standards for Reinsurance*

Reinsurance requires the adoption of national standards establishing the maximum scale of benefits and the minimum level of contributions to be underwritten. This is essential because of a fundamental difference between private and social insurance. In private insurance there is a definite contract between the insurer and the insured, fixing the premiums and the benefits to be paid and defining the conditions under which benefits are payable. But with unemployment compensation, there is no contract. A state unemployment compensation fund is like a bag open at both ends. At any session the state legislature can increase the benefits or decrease the contributions. Obviously, it would be impossible to reinsure a system that could at any time be driven into bankruptcy by changes of state law.

To protect the national reinsurance fund and the rights of other states, it would be necessary to place a ceiling over benefits and a floor under contributions. Otherwise, the fund could deliberately be "milked" to the advantage of a few states, and the whole plan soon would collapse. The following standards would appear to be essential for reinsurance:

(1) A maximum limit upon benefit rates, preferably so designed as to fix the maximum level of benefit rates but to permit the use of any of several formulas for their computation.

(2) A maximum limit on benefit duration, fixed either as a stipulated multiple of the claimant's benefit rate, or as the lesser of the amounts obtained by applying this multiple and by taking a specified fraction of the claimant's earnings during the base period.

(3) A minimum requirement for benefit eligibility, determined by the amount of earnings or the length of employment in the base period, according to the method of computation used in the particular state.

(4) A minimum length of waiting period.

(5) Probably, certain minimum requirements on disqualification for benefits in case of loss of employment as a result of voluntarily quitting, being discharged for misconduct, or being involved in a labor dispute.

(6) A minimum level of contributions, fixed as a ratio of total contribution collections to the aggregate amount of payrolls liable to the state levy for unemployment compensation.

These standards could be sufficiently flexible to leave considerable room for state discretion and experimentation in benefit formulas, experience rating plans, and the like. In spite of a national limit on benefit rates and duration, a state could establish a higher level if it chose to maintain contribution rates greater than those required by the standards, or to levy employee contributions. The main problem would be to keep accounts which would properly separate the benefits chargeable to the required contributions from those financed from additional revenues raised at the volition of the state. Because of the extraordinarily small volume of unemployment to be compensated in the District of Columbia and perhaps in a few other jurisdictions, it might be necessary to permit a state to reduce contributions below the national minimum level if it paid benefits at the maximum limits and had a balance of a certain size in its unemployment compensation fund. Undoubtedly most states would quickly revise their laws to provide benefits up to the maximum limits established for reinsurance purposes, since the cost would be borne by the reinsurance fund if it were beyond the capacity of the state fund. The national standards, therefore, would become in reality both maximum and minimum standards.

### *Financing the Reinsurance Fund*

How could a national reinsurance fund be financed? One method, of course, would be by appropriations from general federal revenues. With the present condition of the federal budget and the heavy demands that are bound to be made on the Treasury in coming years, it seems doubtful whether the necessary sums could be obtained in this manner, especially as it is now an established practice to rely upon payroll taxes to finance unemployment compensation. Another plan would be to levy an assessment upon the states to support the reinsurance fund. A third method would be to increase the yield of the federal unemployment tax by lowering the offset limit below 90 per cent and to credit to the reinsurance fund the proceeds of the tax in excess of the amount required for

grants for state administration. This would involve the amendment of state laws to lower the basic state contribution rate from 2.7 per cent to whatever point the change in the offset limit called for.

In either the second or the third plan, the rate of assessment against the states or the increase in the federal share of the payroll tax should be fixed not merely to meet year-by-year shortages in the weaker state unemployment compensation funds, but also to accumulate a large national reserve for times of depression. Both are essential if the reinsurance fund is to accomplish its purpose. Depression unemployment is peculiarly a phenomenon of the national economic system rather than of the industrial systems of individual states. It, therefore, calls for a nation-wide sharing of the risk and the accumulation of national reserves to meet the abnormal benefit costs of depression years. Only by pooling the depression reserves of the entire unemployment compensation system in a single national fund can the system acquire maximum strength. If these reserves are scattered among a national reinsurance fund and fifty-one state funds of varying degrees of adequacy, the resources of some state funds and of the reinsurance fund may be exhausted while unused balances remain frozen in the funds of a few particularly fortunate states. In consequence, unemployment compensation may break down in the very areas where unemployment is most severe and the need for benefits greatest.

The rate required to build up a reinsurance fund for periods of special stress is, of course, a problem for actuaries rather than laymen to fathom; but for the safety and effectiveness of the federal-state system of unemployment compensation, the doubts should be resolved in favor of too large rather than too small a reinsurance fund. If the share of unemployment compensation payroll taxes assigned to the reinsurance fund is unnecessarily great, the states may have to draw upon it more frequently in ordinary years, but the money will be available when and where needed. If the share is too small, however, the reinsurance fund may become insolvent and benefits may cease in some states while excess reserves remain sequestered in states with light unemployment.

## CHAPTER X

### THE RELATIVE MERITS OF FEDERAL-STATE AND FEDERAL SYSTEMS

IN PLOTTING THE FUTURE course of unemployment compensation administration, three possible alternatives are available. One is to retain and perfect the federal-state system, another is to abandon federal participation and leave the enterprise entirely to the states, and the third, to substitute a national system of administration. The real choice lies between the first and third plans, though a few persons have advocated the second.

Complete state control has little to commend it. It would, of course, eliminate some of the complications and the red tape that are practically inherent in the present arrangement, but at the same time it would remove many of the beams that support the structure. Without the stimulus, financing, and protection which the Social Security Act provides, unemployment compensation would not have come into being throughout the country, and without them it would soon collapse in many states. It is only necessary to look at workmen's compensation to realize the force which the federal Act and the Social Security Board have exerted. After thirty years of effort there is still one state which does not have workmen's compensation; in many others the laws are very inadequate and ineffectively administered. Were federal participation withdrawn, it is probable that unemployment compensation would be discarded in some states. Without the influence of the Social Security Board, its standards and technical service, the quality of unemployment compensation administration certainly would decline. In many states the spoils system would reassert itself and a complicated mechanism would fall into the hands of political administrators. This would mean a high turnover in personnel and breakdowns of service which might discredit the undertaking.

But more fundamental than the probable effects of complete state control on administration is the essentially national character of the problem with which unemployment compensation deals. Unlike industrial accidents, the causes of unemployment largely lie outside the plant where the hazard is met. Nor are they limited to the state. To a great extent they are regional or national. With an economic system national in

scope and an insurance risk largely national in origin, it would seem clear that there should be federal participation in the financing and administration of the unemployment compensation system.

### ADVANTAGES OF A FEDERAL-STATE SYSTEM

In framing the Social Security Act, the most conclusive reason for the adoption of a federal-state system of unemployment compensation was constitutional expediency rather than the fundamental merits of the plan. It was felt that a scheme of this type might be upheld by the Supreme Court, whereas the constitutionality of a national system was considered dubious at best. But the decision of the Court upholding the old-age insurance provisions of the Social Security Act leaves little doubt that national administration of unemployment compensation is constitutionally possible.<sup>1</sup> Consequently, the choice between a federal-state and a federal system now turns upon the relative desirability and effectiveness of the two plans, as it should.

#### *Broader Opportunity for Experimentation*

Constitutionality, however, was only one of the considerations which led the President's Committee on Economic Security to recommend a federal-state system. Among the Committee and some of its technical advisers there was a belief that this plan would be more satisfactory, at least in the early years. Particular emphasis was placed upon the complete lack of experience with unemployment compensation in this country and the need for experimentation to work out the most desirable methods of operation.<sup>2</sup> When the Social Security Act was passed, the relative merits of many of the alternatives in unemployment compensation were little understood and most decisions had to be made on the basis of theoretical analysis.

The greater opportunity for experimentation is unquestionably one of the major advantages of the federal-state system. It permits testing a variety of plans on a limited scale and assures a rapid accumulation of experience, whereas with national administration there would at least have to be uniformity of law. With half a hundred state or territorial laws and an equal number of operating agencies, a large amount of diversity in statutory provisions and in methods is inevitable. Several

<sup>1</sup> *Helvering v. Davis*, 301 U.S. 619.

<sup>2</sup> *Report of the President's Committee on Economic Security*, 1935, pp. 13, 14.

different benefit formulas have already been tried and a number of experience rating schemes developed. Several states are experimenting with special regulations limiting the benefits of seasonal workers—one of the most difficult problems of unemployment insurance in all countries. Two plans of wage reporting have been introduced, and at least three distinct systems with numerous combinations and variations have been developed for handling benefit operations. From a careful analysis of the different plans in use in the states, it should be possible within a few years to determine the most efficient operating methods and to judge, though with much less assurance, the social desirability of various types of unemployment compensation provisions.

But it should not be assumed that a federal-state system is essential to experimentation. A national system necessitates uniformity of law, but it does not require uniformity of operating method. Different plans of organization and procedure could be tested in different regions, and no doubt should be. Failure to experiment is more a reflection upon the imagination and capacity of administrators than an inevitable consequence of unified administration. There is no reason, for example, why all of the existing methods of benefit operation could not satisfactorily have been tried out if unemployment compensation had been set up as a national system. Similarly, national administration would have permitted the use of both of the basic schemes of wage reporting. Once the efficiency of different methods has been tested, national administration makes possible a prompter application of the results throughout the country than does a federal-state system; but in the fields of legislation, regulation, and interpretation, the latter permits much wider experimentation. Yet it must be noted that state unemployment compensation laws thus far have not undergone changes as sweeping as those made in the old-age insurance provisions of the Social Security Act.

#### *Adaptation to Local Conditions*

A second advantage of a federal-state system is that it permits readier adjustment to local conditions. This also was one of the considerations stressed by the President's Committee on Economic Security. It was feared that it might be impossible to devise unemployment compensation provisions properly adapted to the wide differences in industry and in wage levels to be found among the states. It was recognized that a benefit level suitable in the Deep South would be entirely inadequate in New York City, and vice versa.



In so far as the form of unemployment compensation system is concerned, the problem of adaptation to local conditions has its principal significance in dealing with matters which require legislative, as distinguished from administrative, treatment. Both the populous metropolitan centers of the North and East and the sparsely settled areas of the West present administrative difficulties necessitating special adjustments in local organization for unemployment compensation and employment service, but these difficulties can be met satisfactorily by a national agency. After all, no single governmental agency—federal, state, or local—extends into every nook and cranny of the country to as great a degree as the federal postal service. Both the Bureau of Old-Age and Survivors Insurance and the Railroad Retirement Board, as well as the state employment security agencies, have had to devise methods of bringing social insurance to out-of-the-way places.

The geographic differences that most directly affect the provisions of state unemployment compensation laws are those in living costs, frequency of wage payment, and seasonality of employment. In a country as vast as the United States, benefit rates have to be adjusted to the living standards of the particular region. With flat benefit rates, as in Great Britain, this would call for different statutory provisions for the various sections, but with the American plan of relating the benefit rate to the earnings of the individual worker, it does not. In fact, the formula of the Draft Bill, basing benefits on the most recent full-time weekly wage or on the highest quarter's earnings, was accepted in toto by states in both high- and low-wage areas, as it provided an automatic adjustment to the earnings level of the worker.

The frequency of wage payment also varies in different parts of the country and affects the payment of benefits, especially for partial unemployment. In New England most workers are paid weekly, while in some western states semi-monthly payment predominates. In general, it is logical to pay benefits at about the same intervals as workers normally receive their wages, since they are accustomed to planning their spending on that basis. It also helps in the administration of benefits for partial unemployment if the benefit period fits the pay period, because earnings are deducted in computing the benefits. The problem of adjusting benefits to pay periods, however, is not solved by state administration, though its magnitude is somewhat reduced. There is no uniform length of pay period in any state; each has thousands of workers receiving their wages weekly and other thousands, bi-weekly or semi-monthly.

The problem, therefore, has to be solved, if possible, by devising a method for paying partial benefits which operates satisfactorily with any of these pay periods.

The importance of seasonal unemployment and the need for special restrictions on the benefits of seasonal workers also vary greatly from state to state. Oregon probably would bankrupt its unemployment compensation fund without seasonal limitations, while many states can afford to disregard the problem entirely. In general, unemployment compensation administrators prefer to avoid special adjustments for seasonal unemployment if the condition of their funds permits. If that is a sound position to take, the problem would largely disappear under a national system, because of the wider distribution of the risk and the greater strength of the national fund. If special provision for seasonal unemployment were deemed necessary, it could be applied with national administration, as it has been in Europe; but with either state or national administration it creates important complications.

#### *Decentralized Administration*

The decentralization of administration, which a federal-state system automatically provides, has certain advantages. In the first place, it puts authority in the hands of persons who are, or can soon become, familiar with local conditions in the area in which they operate. Though a national system of unemployment compensation would have to function through a number of regional centers, most of the regions would probably be too large to permit officials to acquire the detailed acquaintance with local communities and industrial conditions that state officials often possess. This type of knowledge was especially valuable in setting up the local organization for unemployment compensation and employment service, and it has continuing importance in keeping the agency abreast of local fluctuations in employment. Against the state officials' more thorough familiarity with local factors must be set up the somewhat broader comprehension of the employment security program which the smaller number of officers necessary for federal administration would possess, if properly selected.

State administration also brings the center of operations closer to the worker and the employer. This makes it easier for them to present their problems to responsible administrative officials. Probably more important, it somewhat reduces delay in the payment of benefits by shortening the distance between the local office where claims and continued claims

are taken and the central office where determinations are made and checks issued. The Railroad Retirement Board pays unemployment insurance benefits from ten regional offices with little delay in transit; but this is principally due to the fact that the insured workers reside along railroad lines, thereby facilitating the transmission of mail between the worker's community and the regional office.

Because state officials are nearer at hand and, on the whole, more exposed to local public opinion, they are probably subject to greater pressure for prompt and efficient payment of benefits than federal officials would be. It may, therefore, be contended that state operation will provide better service to the public. On the other hand, state officials and the personnel of the agencies are also more exposed to political pressure than are those of the federal Bureau of Employment Security, and that does not contribute to efficiency.

### *Coordination with Other State Activities*

State operation also permits a closer coordination of unemployment compensation with related state and local activities, particularly with public assistance and the administration of labor laws, though it cannot be said that coordination has progressed very far as yet. In many states the employment security agency is a part of the state labor department, but its operations are little tied in with those of other units of the department, as a rule. Usually the relation seems to have its principal value in placing at the disposal of the agency the knowledge of industrial conditions and labor relations which the head of the department may have acquired. In no state are unemployment compensation and public assistance activities actually administered by the same department,<sup>3</sup> though limited relations have been established between unemployment compensation and relief agencies in most states.

The coordination of unemployment compensation with relief and other public assistance activities presents two principal problems: first, the establishment of a practicable method of clearance by which relief authorities may obtain information on the benefit status of relief clients; and second, the determination of the proper spheres of unemployment

<sup>3</sup> The state of Washington originally established a department of social security, which included unemployment compensation, employment service, and the various public assistance programs, but there was little connection between the two groups of activities in practice. An independent agency was created for unemployment compensation and employment service in 1939. On paper, Minnesota now has a so-called social security department, consisting of divisions of employment security, social welfare, and public institutions, but each of these divisions is administered as an independent agency.

compensation, public assistance, public works, and other programs for coping with unemployment. The clearance of information to relief authorities does not involve special difficulty or require that the two functions be administered by the same department or by agencies on the same governmental level. Reasonably satisfactory procedures have been developed in some states, and in many the purposes of clearance could be achieved by methods much less laborious than those in use. A comparatively simple and effective plan has been devised which permits the clearance to be handled directly between the local relief agency and the employment office.<sup>4</sup> This plan could be applied as readily with national as with state operation of unemployment compensation.

The development of a coordinated program for dealing with unemployment is the basic and by far the most difficult problem of inter-agency relationship in which unemployment compensation is involved. Whether the federal-state system simplifies or complicates this development is not clear. Most of the activities concerned are conducted by state or local governments. On the other hand, because the program must largely be financed by the national government in times of stress, the underlying policies in all likelihood will have to be determined at the national, rather than the state, level. In formulating the policies, it might be simpler if there were a single, uniform system of unemployment compensation for the entire country.

In constructing a program for dealing with unemployment, it would seem that unemployment compensation should be the stable factor and relief and public works the adjustable elements. As has so often been said, unemployment compensation is only a first line of defense against unemployment. If benefits are to be paid as a matter of right rather than charity, and if the system is to be maintained on a sound actuarial basis as nearly as determinable, unemployment compensation has to be viewed as only a first defense and shielded from tinkering that might convert it into a dole. If this conception is accepted, the problem, in so far as unemployment compensation is concerned, narrows down to determining the scope of coverage that should be established and the type of benefit structure which will produce the maximum of socially desirable results from the financial resources of the system. Once conclusions have been

<sup>4</sup> Arthur T. Jacobs, *Methods of Clearance Between Unemployment Compensation and Relief Agencies* (Washington: Committee on Social Security of the Social Science Research Council, Pamphlet No. 3, 1940).

reached on these matters, unemployment compensation can be treated largely as a constant in working out the rest of the unemployment program. If so viewed, it probably makes little difference in state planning whether unemployment compensation is set up on the present or a national basis.

### *Local Participation in Administration of Employment Service*

Another consideration which weighed in favor of a federal-state system when unemployment compensation was introduced was the fact that in many areas employment service, with which it needed to be integrated, was administered by the states. Moreover, there was a belief on the part of many of those interested in employment service that it would be more effective if closely tied in with state and local government. This view was accepted by those who formulated the Wagner-Peyser Act. But now the effort to link employment service with local government has definitely been abandoned in most parts of the country as an unnecessary complication. There is no evidence that the employment offices having this relation are more successful than others. Nor is it clear that state administration results in a more effective employment service than would national administration. It is probably true that many state employment offices provided a better placement service for their communities than did those of the National Reemployment Service, but the difference was due to more adequate and stable financing, which assured a better personnel and a more continuous promotional effort, rather than to the fact of state administration. The National Reemployment Service was frankly an emergency agency, greatly handicapped by unstable financing in its attempt to develop a placement service for private industry.<sup>5</sup>

### ADVANTAGES OF A NATIONAL SYSTEM

For convenience and clarity the advantages claimed for a national system of unemployment compensation may be divided into two groups: those relating to administration, and those of an economic and social nature.

<sup>5</sup> The author bases these comments on an extensive field study of employment service in 1936 when both the state services and the National Reemployment Service were operating. For a further discussion of the matter see Atkinson, Odenchantz, and Deming, *op. cit.*, pp. 24-28.

*Simplification of Administration*

A national system would eliminate the division of authority and responsibility inherent in the federal-state plan and greatly simplify the administration of unemployment compensation. In place of over fifty legislative bodies and a like number of administrative agencies, it would substitute one legislative body—Congress—and one or at most two administrative agencies, the Social Security Board and the Treasury Department. This would fix responsibility which, in a federal-state system, is often very difficult to assign.

Deficiencies in the operation of a state employment security agency may be attributable either to the agency itself or to the Social Security Board, and the public can scarcely be expected to discover the real cause. The Social Security Board can disclaim accountability because control of operations is vested in the states. But state officials can say, and sometimes rightfully, that they are powerless to meet the situation because of federal regulations or inability to obtain the necessary funds. For example, there is no question that the establishment of experience rating accounts was considerably delayed in a number of states by the failure of the Board to provide the grants necessary to finance the work. But more often the Board has been used as a convenient excuse for shortcomings in administration which had their origin within the state.

National administration would eliminate much of the internal friction which characterizes the present arrangement, and would substitute direct administration for the slow and cumbersome processes of negotiation and diplomacy in handling relations between the Social Security Board and the operating agencies in the field. National policies and standards could be directly applied, instead of depending upon persuasion, pressure, and a bit of cajolery for their attainment. There would not be the psychological barrier of states' rights, which now impedes cooperation between state and federal officials. This barrier is a matter of no little consequence. It tends to make agencies unnecessarily jealous of their prerogatives and causes a few to resent suggestions and resist federal regulations regardless of their validity and merit. Over a period of years this obstacle should gradually give way to habits of cooperation and to mutual interest in the success of the program, but it has hampered the development of unemployment compensation thus far.

A federal-state system has far more administrative gears, levers, and gadgets to manipulate than either a national or a state system would possess. To the usual mechanics and red tape of state administration is

added another set imposed by the federal government as a condition of grants. The state employment security officials must operate within the bounds both of their own laws and of the Social Security Act, comply with state regulations and the standards of the Social Security Board, and maintain relations with a considerable group of state agencies and officials as well as with the Board and the federal Treasury Department.

In a state where unemployment compensation is included in the department of labor, the head of the employment security agency must keep the commissioner of labor, as well as the federal regional representative, thoroughly informed on the operation of his agency and must deal with the attorney general, the comptroller, the treasurer, the purchasing officer, and perhaps a state civil service commission and a few other central administrative agencies on matters falling within their respective spheres. Funds for the operation of employment security agencies must be obtained by federal grant on the basis of budgets reviewed and revised by the Social Security Board, and must be expended in accordance with a combination of state and Board regulations. Any departure from the approved budget requires federal approval. Finally, the expenditures are subject to audit both by the Board and the state auditor.

For legal advice the head of the employment security agency normally looks to the attorney general of the state, but he faces the possibility of difficulty with the Social Security Board if, in the judgment of the General Counsel of the Federal Security Agency, the opinion of the attorney general raises a question of conformity with the Social Security Act or may result in the denial of benefits to persons entitled to them. Equipment purchases must be made in accordance with state purchasing regulations and must be individually approved in advance by the Bureau of Employment Security. A change of salary rate requires approval by the Bureau and in many states by the civil service commission or the budget officer. In a few states the leasing of office space involves action by a central agency in charge of the acquisition of real estate as well as by the federal Bureau. In addition to all this, in most states the comptroller and the treasurer participate directly in the benefit payment process, one verifying and approving the payments and the other issuing the checks.

Thus, it may be seen that the heads of state employment security agencies have no simple task. In practice the complications have been somewhat lessened by the tendency of state administrative authorities to relax their regulations in dealing with the employment security agency and

either to exempt it in part from the usual requirements or to be guided in large measure by the wishes of the agency. But this very practice has led to a tightening of federal controls. Many of the difficulties will no doubt be eliminated or reduced as Board policies become more definite and generally understood, and as federal standards are substituted for advance federal approval of individual transactions. Yet in spite of all, a federal-state system inevitably is more complicated to administer than a national system. There remain two sets of laws and regulations, dual overhead supervision, and a considerably greater number of officials and agencies with which state employment security officials must deal in obtaining and expending their funds and operating their agencies.

### *Improvement of Personnel*

It is often said, and probably with justification, that the personnel of the federal government is of a somewhat higher standard than that of the average state. The Social Security Board through its merit system requirements, however, has done much to improve personnel practices and assist the state agencies in obtaining and retaining competent staffs. The relative caliber of the personnel under national, as against federal-state, administration depends largely, however, on the degree to which the special merit systems for state employment security agencies succeed. In states where there is a strong spoils tradition and the general level of administration is low, the maintenance of satisfactory personnel standards is apt to be a prolonged struggle. The occasional disruption of agencies by spoils attack seems inevitable in the light of the history of state administration. While politics and the spoils system are not strangers to federal administration, they do not reach by any means as far down in federal bureaus as in the average state department. In fact, in many bureaus the head himself is under civil service and the staff is very little affected by changes of administration. Stability of personnel, of course, is no measure of ability, but without reasonable stability the maintenance of an efficient organization is impossible. If unemployment compensation is to attract competent persons, it must offer assurance of freedom from political turnover and provide an opportunity for a career.

A national system would have one advantage in developing an effective staff which it will be very difficult to achieve under a federal-state system—fluidity of personnel. National administration would permit a flow of personnel between field operating units and central technical or administrative units, and a ready transfer from one region to another.



The lack of easy interchange of personnel is one of the most serious defects of the federal-state system. This deficiency must be overcome if unemployment compensation is to afford a career and bring to the top the most competent individuals engaged in its administration. Unless it offers opportunity for advancement, the system is bound to lose many of its best people. Some of the ablest young persons engaged in unemployment compensation administration are located in relatively small states with low salary levels. Unless these persons can advance beyond their agencies, they will gradually drop out of the system. Because of state insistence on local residence, it is almost impossible for an official who has succeeded in a small agency to obtain a responsible position in a larger one. The only available avenue of advancement is to the staff of the Social Security Board, and that is limited by the relatively small size of the staff and the requirement that the Board appoint from available federal civil service registers. Thus it cannot promote a person from a state agency to its central office as it can from its own field staff.

This lack of flexibility and opportunity for advancement is harmful both to the state agencies and the Board. It tends to lessen the incentive for state personnel to put forth their best efforts, and it hampers the Board in obtaining the most competent persons for its staff. If, for example, the federal Division of Research and Statistics needs a man with a particular background who is available in one of the state agencies, it cannot transfer him to its staff. Conversely, a technical man in the Bureau of Employment Security cannot be assigned to the staff of a state agency either to acquire needed operating experience or to assist the agency in working out some of its problems. As a result of the gap between the state and federal agencies, the key personnel in the states cannot obtain the breadth of background that they could get through assignment to other areas or to the federal Bureau, and the staff of the Bureau can gain familiarity with operating problems only by observation, not by experience. This limits the horizons and effectiveness of both.

### *More Economical Administration*

A national system would permit some economies in administration through the adoption of larger and more efficient operating units and a partial integration of unemployment compensation and old-age and survivors insurance activities. Though adequate cost data are not yet available, there is sufficient information to establish the fact that the smallest agencies are relatively the most expensive and that, in general, the larg-

est ones have the lowest costs. The principal measure thus far applied has been the ratio of administrative expenses to contributions collected. At one extreme are North Dakota and Nevada with administrative expenses for the year ending June 30, 1940 amounting to 24.5 and 18.6 per cent of contributions, respectively, while at the other end of the scale are Illinois and Ohio with ratios of 5.3 and 5.4, respectively. In recognition of the higher cost level in small states, the Social Security Board has had to make an exception for the very small ones in applying its rule that administrative expenditures must not exceed 10 per cent of contributions. Whereas the big industrial states have had little difficulty in meeting this requirement—most have been considerably under the limit—the sparsely settled states have found it impossible to maintain their agencies on this basis.

If unemployment compensation were nationally administered, most of the activities now carried on by the central offices of state agencies would be concentrated in a relatively small number of regional offices.<sup>6</sup> This would provide larger operating units and reduce administrative expenditures, especially in the less densely populated regions where state costs are now the highest. These savings would result mainly from a lower ratio of overhead to operating expenses and from more efficient use of personnel and equipment made possible by large-scale operation in the handling of central office activities. As a change from state to national control would make little difference in the size and number of employment offices required, no significant economies could be expected in that field. The savings as a result of larger central offices would probably be offset in part by the fact that the federal salary scale is somewhat above the average level of salaries in state agencies.

National administration would also eliminate the waste resulting from separate administration of the payroll taxes for unemployment compensation and old-age and survivors insurance. If both systems of insurance were conducted by the federal government, the three payroll taxes could be combined and administered by one agency, probably with a single tax return from employers.

Nationalization would likewise make it possible to merge the wage

<sup>6</sup> If the Bureau of Internal Revenue continued to administer the payroll taxes, the contribution work performed by state agencies would be shifted to it rather than the Social Security Board. The Bureau has 64 collectors' offices for the administration of all internal revenue taxes. The Social Security Board has twelve regional offices. Assuming that the Bureau of Internal Revenue would administer the payroll taxes, the regional offices of the Board would probably carry on the wage record and benefit operations. The latter activities constitute by far the greater part of the work of the central office of a state agency.

record and reporting systems for unemployment compensation and old-age and survivors insurance, though the method of consolidation presents problems that would require careful study. The Railroad Retirement Board maintains at its central office one wage record system for unemployment insurance and old-age retirement; but a regional system might be necessary for unemployment compensation and old-age and survivors insurance, due to the greater size of the operation and the necessity of speed in handling unemployment compensation claims. Possibly a combination of regional and central records might be desirable. As wage records have an active life of between one and two years for unemployment compensation, it might be feasible to retain them in the regional office until they became inactive for this purpose and then to transmit them to the central office of the Social Security Board for posting to the permanent records for old-age and survivors insurance.<sup>7</sup> If tabulating equipment were used, another plan would be to prepare a duplicate set of tabulation cards from the wage reports, one for the regional office and the other for posting to the central records. Under either scheme employers would be relieved of the preparation of two sets of wage reports, and a considerable saving could be made in the maintenance of social insurance records.

Even with a federal-state system, something could be done to reduce duplication of effort in the administration of payroll taxes and wage record systems and to lessen the cost and inconvenience to employers. But so long as unemployment compensation is operated by state agencies and old-age and survivors insurance by the federal government, separate wage record systems will be necessary. Without experience rating, unified national administration of the payroll taxes might be possible under the present system, though it would be a considerable departure from the federal-state plan of operation. With experience rating, however, dual administration of payroll taxes is apt to remain.

### *Elimination of Interstate and Railroad Problems*

Under a national system the problems of the interstate employer and the multi-state worker would automatically disappear. This would elimi-

<sup>7</sup> If such a scheme were used, the regional office would have to be notified of new claims for old-age and survivors insurance so that it could send the central office a copy of the wage records held by it for the recent period. If the records were held in the regional office during their active life for unemployment compensation, a large part of the errors would have been corrected before they reached the central office for posting to the permanent records.

nate many difficulties in determining employer coverage and would allow the benefit claims of persons with employment in another or in several states to be handled the same as intrastate claims. The only situation in which claims would cause extra work would be where the worker had been employed by concerns reporting in different regions. Here it would be necessary for one regional office to assemble the wage records from the others, but thereafter the transaction would be no different from any other claim. No method has yet been discovered for eliminating all the coverage problems arising with interstate employers under a federal-state system, though most of the difficulties originally encountered have been overcome. The inequities of the system in providing benefits for interstate workers probably can be eliminated, but only by methods which add considerably to the cost and difficulty of handling the claims.

With national administration of unemployment compensation, a separate system of unemployment insurance would not be needed for railroad workers. The main justification for that system was the large proportion of workers with employment in more than one state, which caused considerable confusion in wage reporting and contribution payment in the beginning and resulted in many persons having their benefit rights scattered among several states. Many of these difficulties were eventually removed, but not until after a separate, federally administered insurance system had been established for railroad workers. While railroad employment differs from other employment in a few respects that affect the operation of unemployment insurance, the differences are not sufficient to warrant a separate system if unemployment compensation were nationalized. A merger of the two systems would eliminate the difficulties which arise when workers have both railroad and non-railroad employment.

State boundaries create problems in the administration of employment service as well as unemployment compensation. Many urban areas overlap state lines, but workers are not respecters of political boundaries when seeking jobs, nor are employers in hiring labor. As the jurisdiction of the state employment service is limited to its own state, some additional employment offices have had to be established which otherwise would not have been necessary. More important, state lines have reduced the effectiveness of the employment service as a placement agency. Rightly or wrongly, each state tends to confine to its own jurisdiction the efforts it makes in the clearance of labor. Even in areas such as

Greater New York and Greater Chicago, the amount of interstate clearance is pitifully small in comparison with the hundreds of thousands of workers who daily cross state lines to earn their livelihood. No doubt much could be done through the Bureau of Employment Security to break down the barriers between state services and to obtain a more adequate public placement service for interstate communities, but only with considerable effort. If the employment service were nationally administered, an integrated system of local offices could be established in interstate areas, and in some the work could be better performed with fewer offices.

### *Distribution of Cost of Unemployment over the Economic System*

When one turns from administrative to economic and social considerations, the basic reason for a national system of unemployment compensation is that it more nearly spreads the cost of unemployment over the whole economic system to which the hazard of unemployment is attributable. The state represents only a segment of the national economy—often but a very small one. A large part of the unemployment occurring in a given state is not the product of conditions arising within that jurisdiction, but of forces generated beyond its bounds. Recreation areas have sharp peaks and valleys in employment, not because of defects in the management of local industries, but because at certain seasons of the year vacationists rush into the area from other parts of the country. A coal mining state has heavy unemployment among its miners in the summer, not because of the way in which employers choose to operate their mines, but because the demand for coal in the states it serves declines in warm weather. It is well known that the manufacture of capital goods is subject to especially severe unemployment in times of depression. Obviously, the responsibility for this unemployment rests with the country as a whole rather than with the particular areas in which heavy goods manufacturing is mainly concentrated. Of course, some of the causes of unemployment extend far beyond the country itself. A European war may have grave repercussions on the economic system of the United States. But national administration of unemployment compensation comes as close as is governmentally possible to distributing the risk over the area within which most of the unemployment has its origin.

It should be pointed out, however, that the cost of unemployment can be spread over the country under a federal-state system of unemployment compensation through the medium of reinsurance. The degree to which

this is done depends upon the type of reinsurance scheme applied. The possibilities range all the way from very limited bolstering of insolvent state funds to almost as complete an equalization of the cost as would be achieved under a national system of insurance. But whether anything approximating complete equalization is politically obtainable under the federal-state system is very doubtful.

### *Greater Assurance of Solvency*

By spreading the risk over the widest possible area, a national system would afford the greatest financial strength and assurance of solvency for unemployment compensation. There can be no doubt that some states lack the size and industrial diversification needed to support an adequate system of unemployment compensation. The employment situation in several states is dominated by a single industry—in some a very seasonal industry. Oregon and Washington are cases in point. There, logging and lumbering—both highly seasonal—are the backbone of the insured employment. Michigan, with the automobile industry, affords an extreme example, and several others could be cited. With separate insurance funds, these and similar states must either impose unusually severe limitations on benefits or levy extraordinarily high contribution rates if they are to avoid the risk of bankrupting their funds. In fact, it is very questionable whether some of them could collect contributions at a rate sufficient to pay adequate benefits. Again, reinsurance offers a means of overcoming the deficiencies of a federal-state system if it were applied to the fullest degree.

### *Uniform Treatment of Workers and Employers*

A national system would assure equal treatment of workers and employers under like conditions. In spite of the fact that nearly all the state laws were modeled after the Draft Bill, benefit levels already differ materially. Two members of the same craft having equal earnings but employed in different states may obtain very dissimilar amounts of benefits when out of work, because of differences in the benefit rate formulas, the limits on benefit duration, and the methods of treating seasonal unemployment. Only by the adoption of standard benefit provisions throughout the country can inequities be avoided. This would be accomplished under a national system by the enactment of a single benefit formula for the whole country. With a federal-state system, it could

largely be achieved by the adoption of national benefit standards backed up by a reinsurance plan amounting to practically complete equalization.

Separate state unemployment compensation laws also cause inequities among employers, which will greatly increase as experience rating begins to produce changes in individual contribution rates. Not only are there at least three fundamentally different plans of experience rating now in use, but even among states having the same general plan the detailed provisions differ sufficiently to produce very unlike contribution rates. A sample study of the charge-back method of merit rating—the most widely used plan—as set up in the laws of four states, showed that in some years the same concern would have had contribution rates varying from 0.0 to 2.7 per cent, depending on the state law applied.<sup>8</sup> Such inequities can only be avoided by the adoption of a uniform contribution rate for the entire country or a standard experience rating plan for all states.

### *Prevention of Competitive Reductions in Benefits*

One of the most serious dangers in the existing federal-state system of unemployment compensation is the incentive it offers for states to engage in a competitive reduction of contribution rates and benefit scales. By the revision of the benefit and experience rating provisions of its law, a state can effect substantial reductions in employers' payroll taxes. If such a movement gets under way in a few states, employers in other states will be placed at a disadvantage by the lower taxes paid by their competitors. Then pressure will be applied for similar or greater reductions in these states.

With a national system, interstate competition in destructive amendments could not occur. Changes in the benefit scale and the contribution provisions would have to be fought out in Congress for the country as a whole. There might be increases or decreases, but they would not be forced by interstate competition. Moreover, employer and employee forces are much more nearly equal in strength nationally than they are in a large percentage of the states. That considerably lessens the danger of ill-considered and one-sided amendments.

### *More Adequate Benefits Where Most Needed*

It is one of the paradoxes of the present federal-state system of unem-

<sup>8</sup> Karl Pribram and Philip Booth, *Merit Rating and Unemployment Compensation* (Washington: Social Security Board, 1937), p. 37.

ployment compensation that it permits the most generous benefits in states with the most stable employment, and provides only the most inadequate benefits in those where unemployment is most severe and workers have the greatest need for protection. Other things being equal, the less the unemployment, the greater will be the yield of the payroll tax and the larger the fund available for the payment of benefits. Conversely, the greater the unemployment in a state, and hence the greater the need for benefits, the less will be the return from a given contribution rate and the smaller the fund available for benefits. In more concrete terms, this means that in states whose dominant industries are especially subject to severe seasonal or cyclical unemployment, benefits cannot be as large as in other states, though workers will suffer much greater unemployment and loss of income. The question may well be asked whether that is the result the nation desired to achieve when it established an unemployment compensation system.

#### *Protection Against Conversion into a Dole*

A national system would probably be better able than the present type to withstand efforts to convert unemployment compensation into a dole in periods of severe depression. This is true because it removes the control of unemployment compensation further from the point at which the pressure of relief financing is first and most acutely felt when the country plunges into a business depression. In reviewing the course of the depression of the 1930's, one first witnesses the exhaustion of local resources for relief, then the beginning of large-scale state participation in relief financing, and finally the inauguration of federal relief activities. It is reasonable to assume that, in a future depression following a sustained period of prosperity, events will follow much the same course. When the state government finds itself confronted with the necessity of raising millions for relief and with an insistent demand from hard-pressed citizens for tax reduction, it requires little imagination to realize that some governors and legislatures are going to turn to unemployment compensation funds for the money. There will be a great temptation either to divert the money directly, perhaps by allegedly borrowing it from the fund, or to amend the unemployment compensation law to lower benefit rates and provide for a great extension of the benefit period. Either will soon exhaust the fund and reduce unemployment compensation to relief.



## CHAPTER XI

### SUMMARY AND CONCLUSIONS

THE FEDERAL-STATE SYSTEM of unemployment compensation presents difficult and unusual problems as to the spheres of state and federal agencies and the manner in which their relations should be conducted. Fundamentally, it is a collection of state administered systems subject to advice and a considerable measure of supervision and control by the Social Security Board. Immediate responsibility for operation within any given area rests with the state agency; but as the entire cost of administration is financed by federal grants, the extent of the influence exercised by the Board largely depends upon its conception of its task. The supervision and control it exercises can be so minute as to fall little short of federal administration, or so loose as to place little restraint upon state discretion.

#### FEDERAL FUNCTIONS IN THE FEDERAL-STATE SYSTEM

Considering the nature of the undertaking and the provisions of the Social Security Act, it seems clear that, within the limits of efficient administration, the states should be free to operate their employment security agencies as they deem best. It is not for the Social Security Board to make the decisions for state agencies. Its responsibility is to obtain efficient administration of unemployment compensation by the states rather than to administer unemployment compensation in the states. To that end the Board may aid state officials with their problems and, where the requisites of efficient administration are reasonably clear, it may properly prescribe the use of proved methods or forbid practices which have not succeeded. Basically, the task of the Board is to coordinate and help to develop efficient state employment security agencies to bring about an effective nation-wide system of unemployment compensation and employment service.

The major functions of the Social Security Board in the federal-state system of unemployment compensation may be summarized under six heads:

1. To conduct basic research and developmental work;

2. To provide expert advice and assistance on technical and administrative problems;
3. To establish minimum standards of administration;
4. To review state plans of administration and operation;
5. To pass on budgets and grant funds for administrative expenses;
6. To audit and inspect state agencies.

### *Research and Developmental Work*

Just as the parent company in a great corporate system commonly carries on a large part of the research and developmental work for the entire organization, so in unemployment compensation these functions are to a great degree the responsibility of the Social Security Board. Most of the more fundamental problems needing study and the results of the more important research are pertinent to all or many of the states. It is therefore desirable that these studies be directed or closely supervised and coordinated by the federal agency. Nevertheless, much of the work must be done in the field in cooperation with state agencies, because that is where the raw materials of research are to be found. Especially is this true of studies requiring benefit or experience rating data on an individual case basis. Similarly, the federal agency should take a leading part in the development of new methods and procedures and should analyze and disseminate the results of experimentation.

Within a few years the principal questions of operating procedure may largely have been answered, but the underlying problems of unemployment compensation will only have begun to be explored. What should be the relation between benefit rates and earnings for workers in various wage groups? What is the distribution of normally employed workers according to annual duration of unemployment and annual wage loss at various points in the business cycle, and what light does it throw on the needed duration of benefits? How do different experience rating plans affect employment practices? What are the extent and characteristics of seasonal and partial unemployment? These and a host of other fundamental questions will require years of study.

### *Advice and Assistance*

Advice and assistance are the principal means by which the Social Security Board can raise the operating efficiency of state agencies. The Board is the clearing house of state experience. When confronted with

new or difficult problems, state officials naturally turn to it for expert advice. To the extent that it supplies expert advice, it can largely mold the development of the agencies. Upon the quality of this service depend to a great degree the prestige of the Board and the cooperation it can secure in the states.

To meet the needs of the agencies requires not an especially large but an unusually competent federal staff. Two groups are essential: first, a field force composed of persons of broad experience in unemployment compensation who understand the ordinary problems faced by state agencies and are skilful in dealing with state officials, and second, a central corps of specialists, thoroughly acquainted with particular sectors of unemployment compensation, to aid the states and the regional personnel of the Board on the more intricate problems. The regional representatives, of course, form the backbone of the first group. The second calls for specialists in matters such as contribution collection, wage records and reporting, benefit disqualifications, partial unemployment, seasonal unemployment, experience rating, office machinery, office organization, and a number of other aspects of unemployment compensation administration and operation.

The development of the type of personnel needed to assist the states has been both aided and impeded by the large amount of routine business generated by detailed federal supervision and budgetary control. While this has served to acquaint the regional staff and many of the central office personnel of the Bureau of Employment Security with the fiscal and business problems of the agencies, it has left little time for the study of other types of questions. Like the state personnel, the staff of the Board has had to start from scratch and grow with the program. It has had the advantage of being at the center of the unemployment compensation system through which experience constantly flows from the entire country, but the members located in Washington have had the handicap of distance from the scene of operation. In fact, one of the defects of the federal-state system is the inevitable gap separating the state personnel with its operating experience and the federal staff that often must advise the agencies on problems with which it has only a second-hand acquaintance. This difficulty can now be overcome only by intensive field studies to enable members of the federal staff to obtain the practical background they need within their specialties. Over the years it can be met by recruiting the federal staff from the more capable administrative and technical persons in the state agencies.

*Establishment of Federal Standards*

The fundamental concern of the Social Security Board in the administration of unemployment compensation is effective service at reasonable cost. Consequently, standards of cost and performance are the basic types needed. They are particularly essential in measuring the efficiency of state agencies and determining their budgetary requirements, but they are not the kind with which specific compliance can be required. Minimum standards, in the sense of regulations, relate mainly to the methods which assure efficiency in administering the employment security program. In other words, they have to do with the means of achieving satisfactory standards of cost and performance rather than with the operating results themselves.

Once state accounts have been so designed as to separate central and local office costs and to break the former down according to overhead services and operating activities, unit cost data could be obtained with comparative ease for the half dozen major operating activities which constitute the work of the central office. These data should throw valuable light upon the relative efficiency of different agencies and of various systems of mechanization and procedure. Until such information is available, few requirements can be laid down as to unemployment compensation procedure, and the choice of operating methods will continue to involve a considerable element of guesswork. From the unit cost data it ought to be possible to establish normal cost factors for some activities by types of states. This information would be exceedingly useful in determining grants and help to stimulate increased efficiency in state agencies.

In the sense of regulations, the principal minimum standards warranted at this stage in the evolution of unemployment compensation are those concerning administrative methods. The Social Security Board has made remarkable progress in this field. By requiring adherence to sound and well-tested administrative practice—especially in the selection of personnel—it has taken a basic step toward the development of strong and efficient state agencies. The requirement of a merit system, in particular, will undoubtedly prove a great protection against political pressure and an important aid in maintaining a competent and stable personnel. Its value, however, will largely depend upon the quality of merit system administration in the states. The merit system cannot be expected to accomplish the desired results unless qualified persons are

appointed as examination supervisors and as members of state merit system councils and, in most states, unless the technical service of the Social Security Board is utilized in a large measure.

Board standards likewise provide the basis for an efficient system of purchasing and property control, and cover some of the essentials of fiscal administration. In addition, a uniform system of accounts and a monthly or quarterly plan for the allotment of funds might well be required to assure more adequate financial data and better expenditure control within the agencies. In the field of operating, as distinguished from administrative or management, procedures, there can be few regulations until there is much more definite knowledge of the relative efficiency of different methods.

#### *Plans of Administration and Operation*

In the case of public assistance agencies, the Social Security Board requires the states to file a detailed statement of their plans of administration and operation. These plans present the organization of the agency and its relations with other state authorities, as well as the regulations and procedures governing administrative practices and operating activities. The Wagner-Peyser Act likewise requires states to present plans for the operation of their employment services and makes grants contingent on federal approval of the plan and subsequent observance of its provisions in the conduct of the service.

While no such requirement has ever been made for unemployment compensation, it would seem desirable to require employment security agencies to present detailed plans of administration and operation covering unemployment compensation as well as employment service. A new plan need not be presented each year, but it should be kept up to date by filing amendments, and periodically it should be re-examined and revised. The state plan would help the Board to determine whether its standards were being met and would enable it to counsel states on matters not covered by federal regulations. The plan would also bring together in compact and convenient form a comprehensive statement of the organization and procedure of each agency.<sup>1</sup> In so far as the agencies themselves are concerned, the preparation of the plan would be a valu-

<sup>1</sup> The states are required to file with the Bureau copies of all statutory amendments, court decisions, regulations, etc., relating to unemployment compensation and are expected to submit copies of manuals of procedure; but states differ greatly in the extent to which they have reduced their rules and procedures to writing and have sent the materials to the Bureau.

able experience. It would compel a review and rethinking of methods and should lead to many improvements.

### *Budget Review and Determination of Grants*

The budget is both the basis for federal grants and an expression of the state operating program. To be significant, it must present estimates in detail and should be accompanied by a statement of the work program of the agency. For unemployment compensation, the latter calls for an analysis of the work load for each major activity for the current and preceding years and estimates of the load for the coming fiscal period, with an explanation of the manner in which they were made. In addition, it should include a statement of proposed changes in operation which would affect costs. For employment service, much the same kind of information is needed, together with an explanation of proposed changes of program to improve the placement service.

The budget might well set up central and local office requirements separately, with the former broken down by major activities and the latter by employment offices. If this were done, unit costs could be applied to the central office estimates, and local office requests could be examined in relation to type of office and volume of placement work performed.

With national standards of administration and means of measuring operating costs and performance, grants need not be itemized in order to obtain effective federal supervision and control. By requiring efficient methods and affording generous technical assistance while allowing flexibility in the use of grants, better results ought to be obtained than by binding state administrators to the details of the approved budget. In so far as the central office is concerned, a lump amount for each major activity would be preferable to a grant itemized by expenditure categories. It would also permit setting up a reserve grant to handle abnormal work loads in activities, such as benefit payment, which are subject to unpredictable fluctuations.

### *Audit and Inspection*

The necessity of federal audit of the finances of state agencies supported by federal grants is generally recognized. The audit provides an essential safeguard against the misuse of funds and a means of enforcing federal standards. It also affords an opportunity for constructive service to the agencies on problems of fiscal administration.

More important, however, than the audit of state expenditures is the examination of operations. This has largely been the responsibility of the regional staff of the Bureau of Employment Security, but it also requires specialized personnel working from the central office of the Bureau. For the most part the needed inspection of methods of operation can be carried on incidental to the regular field service, special studies, and technical assistance on state problems. In federal-state undertakings, field service has generally proved more worth while than formal inspection. Inspection is apt to be resented and tends to become routine rather than constructive. The great need is for persons who can advise and assist state officials rather than for those who can merely audit.

Nevertheless, there are some aspects of unemployment compensation administration other than finance which probably need periodic audit. The Social Security Board has already instituted an audit of personnel activities to determine whether its merit system requirements are observed and to aid states in improving their personnel procedures. It might also be worth while to have a periodic sample audit of benefit determinations for accuracy of the computations and for validity of the decisions on questions of disqualification. An audit of this kind would undoubtedly reveal a substantial percentage of error in the calculation of benefits and many cases of injustice in the disposition of claims, and would induce greater care and fairness in the operation of unemployment compensation.

#### PERFECTING THE FEDERAL-STATE SYSTEM

It is not surprising that there are gaps in the federal-state system of unemployment compensation at this early stage in its development and that there are gears which do not properly mesh. With so many laws and administrative agencies involved, it will require considerable time to perfect the system. Some of the difficulties relate to administrative coordination and some to weaknesses in the compensation structure due to the multiplicity of parts forged by independent legislative bodies.

The administration of state and federal payroll taxes presents one of the major problems of coordination. With thousands of employers paying unemployment compensation levies in more than one state, and with all but the smallest employers subject to three payroll taxes administered by two agencies—one state and one federal—coordination is essential both for the convenience of taxpayers and for efficient administration

of the taxes. A basic step in achieving better coordination would be the extension of the coverage of unemployment compensation levies and the federal unemployment tax to equal the coverage of the federal tax for old-age and survivors insurance. More consultation among federal and state agencies on the interpretation of coverage provisions would also produce greater uniformity. Perhaps final authority on federal coverage issues should be vested in the Social Security Board which now handles such questions arising in the determination of claims for old-age and survivors insurance, while the Bureau of Internal Revenue disposes of similar issues in the enforcement of federal payroll taxes.

A two-way clearance of information between state agencies and the Bureau of Internal Revenue would contribute to the effectiveness of both. An interchange could be maintained on new employers and concerns ceasing business and on the results of field audits and investigations which disclose additional taxable payrolls. In view of the numerous complications which individual employer experience rating would add to a system of unified tax administration, these expedients appear to offer a more practicable means of simplifying and improving the administration of the payroll taxes than the establishment of a single national tax for unemployment compensation.

Wage reporting and record keeping also provide worth-while opportunities for coordination among social insurance agencies. The adoption of uniform wage-reporting forms for unemployment compensation and old-age and survivors insurance would greatly reduce the employer's burden in preparing reports. With a modification of the base period commonly used in computing unemployment benefits and a small change in the benefit formula for old-age and survivors insurance, it would be possible to substitute annual for quarterly wage reporting for employers with satisfactory payroll records. Annual reporting would greatly reduce the wage record work of unemployment compensation agencies and the Bureau of Old-Age and Survivors Insurance. It would also permit the adoption of a uniform wage-reporting blank which would meet the needs of unemployment compensation, old-age and survivors insurance, and the Bureau of Internal Revenue and permit employers to produce the three reports at one operation.

Unemployment compensation is not yet properly geared for the payment of benefits to workers who have been employed in two or more states, or who have had both railroad and non-railroad employment. Because the compensation laws do not mesh, these workers may either



suffer a serious loss of compensation or obtain benefits from two or more agencies considerably in excess of the amount they would have been entitled to had their employment been entirely covered by one of the laws. These defects could be overcome if the states would amend their laws to have the claims of interstate workers determined and paid by the state receiving the claim, subject to reimbursement by the other states concerned.

To assure an adequate benefit structure in the states, it is important that the Social Security Act be amended to establish national minimum standards for benefits and contributions, as a condition of state eligibility for grants. The facts must be recognized that, in many states, unemployment compensation came into existence because of the Social Security Act and that without strong federal support it may be emasculated by hostile amendments to state laws. In most states the benefit system falls considerably short of achieving the objectives of unemployment compensation, though in many a contribution rate of 2.7 per cent would permit a higher benefit scale than now exists. The greatest need is for a longer duration of benefits more nearly sufficient to carry workers through their annual periods of unemployment.

But adequate benefits cannot be maintained in all states over a period of years without reinsurance to spread the risk over the entire unemployment compensation system and supplement the weaker state funds. A federal reinsurance fund, on which states can draw when their reserves become exhausted, is essential to a strong and effective federal-state system of unemployment compensation. To protect the reinsurance fund against abuse, it would be necessary to enact national standards placing a maximum limit on benefits and fixing a minimum level of contributions.

### NATIONALIZATION OF UNEMPLOYMENT COMPENSATION

While many of the deficiencies of the federal-state system of unemployment compensation can be overcome, it nevertheless will remain a cumbersome and probably an inadequate system for the administration of unemployment insurance. At the time it was established, it seemed the only plan that would be upheld by the Supreme Court. But now that the constitutional barrier to a national system has been removed, the problem of how to administer unemployment compensation deserves careful reconsideration on its merits.

It is natural to assume that in a country as large and varied as the United States, a single plan of unemployment compensation could not be devised which would take adequate account of differences among areas and be properly adjusted to the needs of each. But this is not the case. As a matter of fact, nearly all the states have modeled their unemployment compensation laws almost entirely upon the Draft Bill prepared by the Social Security Board. While the state laws have been amended in a number of respects, the basic features of the Draft Bill as revised have proved adaptable to conditions in all parts of the country. By basing the benefit rate of each individual upon his own previous earnings, the benefit formula used in the Draft Bill automatically adjusts to differences in wage levels and living standards in the various areas.

The Railroad Retirement Board and the Bureau of Old-Age and Survivors Insurance have already demonstrated the practicability of national administration of social insurance. Though old-age and survivors insurance does not present as complex administrative problems as unemployment compensation, those encountered by the Railroad Retirement Board in the conduct of unemployment insurance for railroad workers are similar in nature to the ones faced in the operation of unemployment compensation. True, the administration of unemployment compensation requires a decentralized organization, but this can be achieved in a national agency by regionalizing its operations, as the Railroad Retirement Board has done with its system of unemployment insurance.

The one really important advantage which the federal-state system possesses over a national system is the greater opportunity it affords for experimentation. This advantage relates more to matters of legislation than to those of administration, for a national agency can try out various methods of operation in its local units. But even in the field of legislation, the advantage is of limited significance. If the federal-state system is strengthened by an effective plan of reinsurance, national standards of benefits and contributions must be adopted which will tend to become both maximum and minimum standards and will greatly restrict the possible experimentation in state legislation.

The advantages of a federal-state system are greatly outweighed by those of a national system. A national system would facilitate simplifications which cannot be achieved under a federal-state plan. It would permit larger and more economical operating units and substitute a single responsible agency for the complex network of agencies now controlling the administration of unemployment compensation. It would

bring about unified administration of the payroll taxes and permit either a complete or a partial merger of the wage record and reporting systems for unemployment compensation and old-age and survivors insurance. Both of these changes would save money for employers and involve substantial reductions in administrative costs. Furthermore, nationalization would avoid the complicated problems arising from interstate employment. It would also make possible consolidation of the unemployment compensation system and the railroad unemployment insurance system and thus would eliminate further difficulties in the present arrangement.

But the fundamental reasons for nationalization are economic and social rather than administrative. With a national system, the risk would be spread over the economic system of the whole country. This would provide far greater financial strength and distribute the burden more fairly. Workers and employers in all parts of the country would receive like treatment under like circumstances. Workers in the states most subject to severe unemployment would not be forced to accept a lower level of benefits than those in areas with more stable industries where the need of compensation is less. Employers would not be subjected to unequal interstate competition due to differences in state experience rating schemes, and this threat to the maintenance of adequate benefits would be removed.

Though it might be possible by the adoption of national standards and reinsurance to accomplish much the same economic and social results as those obtained by an outright national system, the objectives could be much more simply and surely achieved by nationalization. The very measures required to remedy the defects and close the gaps in a federal-state system would tend for the most part to render it more complicated and cumbersome. The needs of the country could be served better and more efficiently by a single national system of unemployment insurance, with unified administration of payroll taxes and a largely unified system of wage reporting and record keeping for unemployment insurance and old-age and survivors insurance. Quite possibly it would be less difficult to substitute a national system than to overcome the defects of the existing federal-state system. But if so fundamental a change is not politically feasible, it is essential that an effort be made to strengthen and perfect the present system by the adoption of national standards concerning the contribution and benefit structure and by the establishment of an effective plan of reinsurance.

## APPENDIX

### PRINCIPAL SUBSTANTIVE FEATURES OF THE UNEMPLOYMENT COMPENSATION SYSTEM

THOUGH STATE unemployment compensation laws differ in many details, the provisions of most conform closely to a single general pattern. The principal features of the compensation system<sup>1</sup> may be summarized as follows:

*Coverage.*—The unemployment compensation system extends to nearly all regularly employed persons other than those engaged in agriculture or in domestic, maritime, or governmental service or family employment and those employed by educational, charitable, or religious organizations not operated for profit. For convenience in administering the payroll tax, most states also exclude persons whose employers have fewer than a specified number of workers—usually between four and eight—but eleven states make no such exclusion.

*Contributions.*—Unemployment compensation is almost entirely financed by payroll taxes. Most states levy a tax—termed a contribution—on employers at a basic rate of 2.7 per cent of their payrolls. A few also require contributions by employees. These are usually levied at the rate of 1 per cent of earnings and are collected through the employer as a deduction from wages. Originally ten states provided for employee contributions, but five have since abandoned them. Employee contributions have little effect on the problem of administration as they are simply added to the employer's return. Their principal effect is on the amount of benefits that can be provided and on the ultimate incidence of the taxes by which benefits are financed.

*Experience rating.*—In forty states, employers' contribution rates are subject to adjustment from the 2.7 per cent base according to their unemployment experience. The purpose of these provisions is to encourage the stabilization of employment and to assess the cost of benefits more largely to the employers supposedly responsible for the unemployment. The methods of experience rating, as this process is called, are various. Most states use the amount of benefits paid to former workers as the criterion of unemployment experience, but with numerous differences in the formulas by which rate adjustments are computed. Several states take as the measure the amount of wages paid within a stipulated period to workers who have drawn benefits. One state uses the number of compensable separations, that is, the number of times insured persons have become unemployed and drawn benefits. Experience rat-

<sup>1</sup> For a detailed discussion of the principles and procedures of unemployment compensation, see Walter Matscheck and Raymond C. Atkinson, *Problems and Procedures of Unemployment Compensation in the States* (Chicago: Public Administration Service, 1939).

ing necessitates considerable additional accounting and somewhat increases the difficulty of administration.

*Reserve funds.*—In most states all contributions are credited to a single reserve fund from which benefits are paid. This arrangement is known as the pooled fund plan. In three states each employer's contributions are set up as a separate reserve account available only for the payment of benefits to his own employees. Four states have a combination of the two schemes. The first plan assures the full payment of benefits to all workers so long as the system remains solvent, whereas the second may result in the non-payment of benefits to employees of concerns with particularly severe unemployment. The object of the individual reserve account plan is to make each employer responsible for the cost of his own unemployment and, by varying his contribution rate according to the condition of his account, to create an incentive to stabilize his employment. Substantially similar results can be achieved with less danger of non-payment of benefits by a combination of the pooled fund plan and experience rating. Most states have chosen the latter approach, and the states with individual employer reserve accounts have now established small pooled funds for the payment of benefits when individual accounts become exhausted.

*Benefit eligibility.*—To be eligible for benefits, a worker must have had under most laws at least a specified minimum amount of insured employment during the preceding year, termed the base year, usually measured in earnings. This minimum varies from a negligible sum in a few states to as high as \$300 in California, but ranges between \$100 and \$200 in most states. The purpose of this requirement is to eliminate persons who are not regularly attached to the labor market and, therefore, not properly entitled to compensation when out of work. Further, the unemployed worker must register with the employment office for placement, file a claim for benefits, and serve a waiting period of two or three weeks before he becomes entitled to compensation, but only one waiting period is required in a year. Unemployment resulting from labor disputes is not compensable. A worker is temporarily disqualified for benefits if he has failed to accept suitable employment, or has voluntarily quit his job without good cause, or been discharged for misconduct. However, he has the right to appeal from the initial determination in these cases and to have a hearing before a referee or appeals tribunal.

*Benefit rate.*—In all but two states benefits are paid on a weekly basis. The benefit rate for a week of unemployment is generally determined either by taking one-half the worker's most recent full-time weekly wage or by using a stipulated fraction (one-twentieth to one-twenty-sixth) of his earnings in the quarter of highest earnings within the preceding base year. In either case the aim is to fix the individual's benefit rate as nearly as practicable in proportion to his earning rate when fully employed—usually at about half that amount. This principle is followed to adjust benefit payments to the income level and

standard of living of the worker and to avoid the possibility of benefits' exceeding normal earnings. The application of this principle, together with the earnings requirement for eligibility and the method of fixing the duration of benefits, necessitates the maintenance of an elaborate system of wage reporting and record keeping, which constitutes one of the major activities of the central office of an employment security agency. A few states base the benefit rate on the claimant's annual, rather than his weekly or quarterly, earnings. This plan makes little difference in the amount of work for the agency, but produces benefits which bear a much less definite relation to workers' full-time earnings than those produced by other types of formulas.

*Partial unemployment.*—All but four states provide benefits for partial as well as total unemployment. Under the common definition a person is partially unemployed in any week in which he experiences reduced working hours and earns less than his benefit rate for total unemployment or an amount \$2 or \$3 greater. The benefit for a week of partial unemployment is the difference between actual earnings and this amount. The small additional allowance provided in most states is designed to make partial employment financially more advantageous than benefits for total unemployment. The payment of benefits for partial unemployment is essential to an adequate system of unemployment compensation, but it presents problems which increase the difficulty of operation.

*Duration of benefits.*—The maximum duration of benefits is limited by law to from thirteen to twenty weeks of total unemployment, according to the state. The most usual limit is sixteen weeks. Benefit duration is further restricted in most states by a provision that the aggregate amount of benefits payable to any worker during a twelve-month period (benefit year) shall not exceed a certain fraction (one-third to one-sixth) of his earnings in the preceding base year. This provision reduces the possible duration of benefits for a large percentage of the workers. To make these limits effective, it is necessary for the state agency to keep a ledger account of the benefits paid each person.

*Payment of benefits.*—To obtain benefits, the worker must file a claim and must report to the local employment office each week to prove his unemployment and indicate whatever earnings he has had. A statement, termed a continued claim, is forwarded each week to the central office, which then issues a benefit check. In a few states these checks are distributed by the employment offices, but in most areas they are delivered by mail from the central office. This procedure contrasts with the European practice of payment in cash at the local office, but permits much greater centralization and mechanization of the accounting and payment process and probably results in more economical operation.

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