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The Employment Service-Unemployment Insurance Partnership: Origin, Evolution, and Revitalization

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ABSTRACT

This study traces the origin and evolution of the partnership between the employment service and unemployment insurance programs in the United States. We examine objectives of the framers of the Wagner-Peyser and Social Security Acts that established these programs. Using primary sources, we then analyze early actions of the architects of social insurance to facilitate cooperation between the two programs to meet economic exigencies, grapple with political cronyism, and surmount legal barriers. We also discuss factors that caused changes in the employment service–unemployment insurance partnership over time. We identify reasons for the erosion in cooperation starting in the 1980s, and explain why ever since there has been a continuous decline in service availability. Reviewing evidence on the effectiveness of in-person employment services for unemployment insurance beneficiaries, we suggest ways to revitalize the employment service–unemployment insurance partnership. We explore the source of Wagner-Peyser Act funding, how it was formalized, then eroded, and how it can be renewed.

JEL Classification Codes: J65, J68, H83

Key Words: employment service, unemployment insurance, Wagner-Peyser Act, Social Security Act, social insurance, public policy, Federal Unemployment Tax Act (FUTA), taxable wage base, intergovernmental relations

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necessarily those of the W.E. Upjohn Institute for Employment Research, U.S. Department of Labor, or any other organization.

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The public employment service (ES) and unemployment insurance (UI) are essential to maintaining robust American labor markets. Established by the Wagner-Peyser Act of 1933 and the Social Security Act of 1935, respectively, these programs were the first permanent federal laws addressing the problem of unemployment in an American industrial society where workers are separated from the sustenance provided by land. Both programs were structured to expand economic security using an approach to federalism that instituted a federal-state cooperative system. The federal government provided grants-in-aid (referred to as “grants”) to states to administer programs of UI and ES under state laws. Under UI, workers who lose their jobs involuntarily are provided partial wage replacement to support reemployment efforts. Employers benefit from UI by keeping skilled workers attached to their businesses during periods of slack product demand.¹ Employers benefit from ES by having a reliable means of canvassing local registries for qualified new workers and ensuring that UI beneficiaries are actively seeking work. By emphasizing reemployment for beneficiaries, the social insurance character of UI is maintained and the moral hazard risk is reduced—the risk is that payment of cash benefits during joblessness might unnecessarily prolong unemployment.

Four broad topics are explored in this study. First, we describe the origin and evolution of the ES-UI partnership and decisive efforts to unify the two programs at the federal and state levels of government. Second, we explain how the partnership matured as policymakers sought to secure a normal order of funding to support the national system of employment offices (now referred to as American Job Centers [AJCs]) through cycles of policy and population preferences. Third, focusing primarily on ES, we show how over the past four decades the

¹ Preventing unemployment was one of the original objectives of UI architects, and maintaining employer–employee attachments by preventing dispersal of an employer’s workforce was the practical policy enunciated by the U.S. Department of Labor (Blaustein 1993, pp. 43–64).

partnership has acquired added service mandates despite chronic reductions in ES resources. These reductions in real funding have curtailed staff-assisted assessment (interviewing, testing, and counseling), job search assistance (JSA), and job finding and placement services, and also diluted ES-UI coordination.² We explain that while technology has offered enormous job finding capabilities, it often has been deficient for many long-term UI claimants, who are exhausting unemployment benefits at higher rates before securing new work. We also summarize several objective research studies providing evidence that public employment services for UI claimants are highly cost-effective. Finally, we suggest policy remedies to revitalize the ES-UI partnership based on the proposals of others and our own research, thoughts, and experiences with the programs.

ORIGIN AND EVOLUTION OF THE ES-UI PARTNERSHIP

The idea for a social security program in the United States emerged in the Progressive Era of the early twentieth century. Finally, during the Great Depression of the 1930s, elements of social insurance were enacted into federal law. A national network of public employment offices was established, along with a program for partial income replacement to the unemployed that provided a safety net for jobless workers (Reich 2010, p. 44). Curt Harding, an architect of the Utah Employment Security Agency, summed up the economic security history of that period, saying it “was part of a reform that was needed in order that the free enterprise system might continue” (U.S. Department of Labor [USDOL] 1985, p. 1). While some European countries nationalized industries and others expanded public assistance to the needy, the United States

² On average, just over half of UI claimants by year obtain at least one staff-assisted ES service (West et al. 2016, p. 15).

established social insurance. Within the panoply of other New Deal reforms and programs, the introduction of employment security programs helped save American capitalism.³

In the late 1930s, federal ES and UI policymakers sought to operate partner programs out of necessity. A report from the Committee on Economic Security (CES), prepared by a White House working group, is the seminal document on social insurance policy in the United States.⁴ Baldwin (1993, pp. 31–32) observes that the 1935 CES report recommended a program of employment assurance before suggesting a program for UI. In Baldwin’s view, this was an attempt to emphasize reemployment after job loss and resulted in ES offices being designated as the points of service for UI claimants.⁵ Thus, the expectation of continued public support for reemployment efforts during periods of UI receipt gave birth to the ES-UI partnership.

BEGINNINGS OF THE ES AND FUNDING

Ordered by President Franklin D. Roosevelt in 1933 to revitalize the federal U.S. Employment Service (USES) right away, Labor Secretary Frances Perkins instructed staff members to begin helping states enact ES laws consistent with the Wagner-Peyser Act, affiliate (certify) state agencies with the USES, and distribute ES grants to states (Perkins 1946, p. 179).

Under the Wagner-Peyser Act, the network of ES offices was administered by states and funded by the federal and state governments on a 50-50 matching basis. During the initial stage

³ The term *employment security* was the invention of Arthur Altmeyer, chairman of the Social Security Board. President Roosevelt’s Reorganization Plan No. 1 of 1939 created the Federal Security Agency. Within the agency, a new bureau was formed containing the Social Security Board and the U.S. Employment Service. Altmeyer named it the Bureau of Employment Security to unite the ES and UI programs (Blaustein 1993, pp. 175–176). *Employment security* is likely a derivative of *social security* and *economic Security* (the original term used by Roosevelt to introduce social insurance).

⁴ The president initiated the CES to study social insurance at the suggestion of the Secretary of Labor (Perkins 1946, p. 279). The membership included the Secretaries of Labor, Agriculture, Treasury, Attorney General, and Federal Relief Administrator.

⁵ See also Balducchi (2011) for an analysis of the CES’s recommendations.

of USES growth, recruitment of unemployed workers to fill job openings for public works projects necessitated setting up temporary federal reemployment offices (called National Reemployment Service [NRS] offices), financed 100 percent by the federal government.⁶ These federal NRS offices also assisted with job finding and placement. To supervise the national build-up of ES offices, a separate division of the NRS was organized within USES (USDOL 1953, p. 12).

As states affiliated with the USES and received Wagner-Peyser Act ES grants, NRS offices were either closed or transferred to state administration. In 1933, there were 158 ES offices and 3,270 NRS offices nationwide. By 1938, the balance was reversed, with 1,263 ES offices and only 188 NRS offices. From 1933 until the early part of FY 1938, the ES system was financed by five different fund sources: the biggest source was NRS allotments from federal public works appropriations, but there were also state appropriations, local government appropriations, Wagner-Peyser Act ES grants, and facilities or staffing contributions from local governments (USDOL 1953, p. 13).

RECESSION OF 1937–1938 SPURS UI-ES PARTNERSHIP

Unemployment declined in 1934, the year after President Roosevelt took office, but recovery from the Great Depression was not continuous.⁷ A new economic downturn started in May 1937 and lasted until June 1938. Unemployment reached over 20 percent with 11 million unemployed (Burns 1956, p. 324; Waiwood 2013). The economic recession of 1937–1938 had an enormous impact on the emerging federal-state ES and UI programs. The Social Security Board,

⁶ These projects were launched under the National Industrial Recovery Act, the Civil Works Administration, and in 1935, the Works Progress Administration.

⁷ This section draws from Friedman (1948).

which administered the nascent UI program, and the U.S. Department of Labor (USDOL), which administered the fledging ES system, began discussions to gather resources to help states expand the network of ES offices.

The CES report had advised states to pay unemployment benefits only through ES offices according to provisions in the Wagner-Peyser Act (CES 1935, p. 19).⁸ Immediately after the Social Security Board was organized, it decided to accept the CES advice (Blaustein 1993, p. 156). The board believed that idled claimants should be offered publicly posted job openings. It also sought to bolster the public image of UI as an earned entitlement rather than a dole involving a means test and opted not to pay benefits out of state welfare offices.⁹ The decision flowed from an overarching New Deal policy that sought to establish permanent federal-state programs to ameliorate unemployment, and findings from the CES report that saw unemployment benefits as a temporary income support paid only when suitable jobs were not available. The latter are foundational elements of social insurance distinct from relief. Every state provided for ES offices to administer UI payments.

The USDOL and the Social Security Board agreed in 1937 that an expanded system of ES offices was needed to meet the demands of the UI program.⁹ Expansion came after intense discussion among policymakers involving valid misgivings. Some USDOL policymakers

⁸ The Social Security Act mandates as a condition of conformity with state UI laws that benefits must “be paid through public employment offices or such other agencies as the Social Security Board may approve.”⁹ The South Dakota legislature adjourned in early 1939 without appropriating funds to match the Wagner-Peyser Act ES grant. The state proposed to pay unemployment benefits through the state welfare offices instead of state ES offices. The board withheld South Dakota’s UI administrative grant until the state came into compliance. By September, the legislature provided matching funds for the Wagner-Peyser Act, state ES offices were reopened and the UI grant resumed (Rubin 1983, p. 175). Under the Workforce Innovation and Opportunity Act (WIOA), individuals with multiple needs must have access to services at AJCs, including the Temporary Assistance for Needy Families program. It would be interesting to speculate on reactions of the framers of the ES and UI programs to this development.

⁹ Of the over 30 states in March 1936 had affiliated with the USES, only 11 had matched funds to the upper limit of federal Wager-Peyser Act ES grants available to them (McKinley and Frase 1970, p. 302).

believed too rapid a build-up of state ES offices could lead to hiring incompetent ES staff, which could result in partiality and a lack of professionalism in administration, with severe adverse public consequences. This perspective was not without merit given the patronage systems operating in many local and state governments.

After state ES laws¹⁰ were enacted, Secretary Perkins' hand-picked director of the USES, Frank Persons, proceeded cautiously to partner with some states.¹¹ There were nine states in 1937 where affiliation with USES was withheld. In those states distribution of Wagner-Peyser Act ES grants and the closing of NRS offices were delayed, in most instances because of political issues surrounding the administration of ES agencies (USDOL 1937a).¹² For example, in Massachusetts, where the ES director was an appointee of Governor James Curley, Director Persons believed the Massachusetts appointee was too weak to resist patronage pressures (McKinley and Frase 1970, p. 295).¹³ Most striking was that of the 35 states affiliated with USES in 1936, only 9 were attempting to provide services within the state.¹⁴ The other 26 states had yet to set up ES offices outside larger cities (USDOL 1953, p. 12).

¹⁰ State ES laws included authorization for or appropriation of matching funds. In the states of Kansas, Maine, Maryland, Michigan, Mississippi, Montana, South Carolina, Utah, Washington, and Wyoming, legislative acceptance of the Wagner-Peyser Act was included in their UI laws (USDOL 1937a).

¹¹ Incrementalism is a trait of federalism. Stepwise adoption of ES by states and USDOL validation was a harbinger for later ES-UI policy initiatives. For example, the national WPRS system was enacted into federal law in 1993 and required concomitant state compliance. Not until June 1996 did all states implement WPRS systems (Robinson 1996, p. 11).

¹² The states were Massachusetts, Pennsylvania, Ohio, Virginia, Illinois, Missouri, Oklahoma, Minnesota, and Colorado.

¹³ From the outset, a professional cadre of employees of state government was indispensable to avert favoritism or corruption by private interests in classifying and referring job seekers. After state ES laws were enacted and the states affiliated, USDOL continued to uphold standards of professionalism. The Iowa ES agency in March 1935 was warned that not adhering to merit standards would jeopardize its Wagner-Peyser Act ES grant. In August 1935 USDOL suspended Missouri's Wagner-Peyser Act ES grant for violation of merit staffing. Not until 1998 in Michigan was another state's Wagner-Peyser Act ES grant suspended for violating federal standards, which included merit selection rules (Balducci and Pasternak 2004; *Michigan v. Herman* 1998).

¹⁴ By May 1937, 44 states had adopted UI laws.

Frank Persons and others argued against consolidated UI and ES activities because it might be harmful to placement activities and hinder participation by employers. While there was sympathy for this view, it was ultimately not shared by Secretary Perkins and the Social Security Board (McKinley and Frase 1970, pp. 298, 305). The relationship between ES and UI raised a host of new policy issues in public administration. These issues necessitated an exchange of viewpoints among remarkably capable New Deal public officials.

Policymakers understood that the Social Security Act would radically expand the mission and volume of ES operations. The policy dilemma facing USDOL and the Social Security Board in 1937 was that the Wagner-Peyser Act authorized neither money for UI activities nor the carrying out of UI activities by the state ES (USDOL 1937b, p. 5). However, the Social Security Act permitted the funding and carrying out of UI activities by the state ES. The administrative challenge was to obtain agreement between the secretary and the board on how to connect federal ES and UI funds, and then figure out how states were to coordinate ES and UI functions within ES offices. Meeting the challenges of the recession required a formal collaboration between two federal agencies, USDOL and the Social Security Board, to successfully enlarge the national network of ES offices and coordinate the UI and ES programs.

POLITICAL CONTEXT AND AGREEMENT OF 1937¹⁵

Getting government agencies to collaborate is always a daunting challenge. Perhaps more so because when Congress enacted the Social Security Act, it authorized the board as an

¹⁵ We will refer to it as the Secretary-Board Agreement.

independent agency, outside of USDOL. According to Perkins, legislators did so because they did not want USDOL to acquire additional responsibilities and resources (Perkins 1946, p. 300).

Therefore, the political context for the agreement included the following:

- The recession was causing unemployment to rise again with fears of another structural breakdown. Thirty-two states (in addition to Wisconsin) were to start paying unemployment benefits in 1938 (USDOL 1937b).¹⁶ Payment of UI benefits in each state required establishing standard administrative procedures for determining eligibility, paying benefits, and certifying for continued job search.
- The recession produced rising political pressure to increase access to services for the jobless. There were large service gaps in helping the unemployed file UI claims and locate work, and Wagner-Peyser Act ES funds alone could not expand service capacity for the burgeoning UI program (McKinley and Frase 1970, p. 306). The fledgling ES system required rapid completion and expansion of ES offices statewide in each state.
- A novel financial relationship between two federal agencies, the USDOL and the board, was essential for the success of the untested federal-state ES and UI programs.

A policy agreement, dated March 30, 1937, between Secretary Perkins and Board Chairman Arthur Altmeyer established coordination and integration of the functions between the two federal agencies. The agreement created a type of “unified service and financing pact,” but it did not govern state operations. According to the agreement, the two federal agencies, the Bureau of Unemployment Compensation (within the Board) and USES (within USDOL), were to

¹⁶ At the time, 32 was the number of states used in memoranda prepared by the Social Security Board. A later article provides a different number (USDOL 1955, p. 51).

- “act as if they were a single agency” with respect to all matters affecting state ES agencies, including state plans funded under the Wagner-Peyser Act and the Social Security Act (USDOL 1937c, 1953, p. 19);
- expand state ES offices and prepare for the payment of UI benefits (USDOL 1937b);
- regard the state agency ES and UI systems as a “unified service” (USDOL 1937d,e);
and
- use UI grants under Title III of the Social Security Act to expand public ES offices, administer benefit payments, and maintain standards of the USES (e.g., merit standards). Such UI grants were in excess of ES grants (USDOL 1937d).

The board interpreted the requirements of the Social Security Act to allow UI grants to support ES. This interpretation was based on the intent of the CES report and the board’s subsequent selection of state ES offices to administer UI payments (Haber and Murray 1966, p. 104).¹⁷ An opinion from the comptroller general of the United States in July 1937 affirmed the board’s decision (Atkinson, Odencrantz, and Deming 1938, p. 55). The USDOL and the board required states to appropriate funds to match Wagner-Peyser Act ES grants before they could receive UI grants.¹⁸

The Secretary-Board Agreement formalized the ES and UI partnership. It was an improvised interdepartmental arrangement, which allowed UI grants to supplement ES grants and state resources to build and maintain a national ES system.¹⁹ Under the Secretary-Board

¹⁷ The board also cited testimony of January 21, 1935, of Edwin Witte, executive director of the CES before the House Ways and Means Committee (McKinley and Frase 1970, p. 302).

¹⁸ A technical resolution adopted in May 1937 governed the operating mechanics of the Secretary-Board Agreement (USDOL 1937d).

¹⁹ A UI grant for the ES was first made to Wisconsin in 1936 and in other states in mid-1937 (Atkinson, Odencrantz, and Deming 1938, p. 197).

Agreement, both ES and UI services were provided jointly in ES offices. While ES and UI functions were unified at a single point of service, ES and UI grants were not comingled. Both USDOL and the board made federal grants available during FYs 1936–1938 for establishing and maintaining ES offices, and to coordinate ES and UI activities. During 1938, 9.2 million initial UI claims were filed, and ES made 2.7 million nonagricultural job placements (Haber and Kruger 1964, p. 29). By the end of FY 1939, the plan to expand ES offices was completed in the 48 states, District of Columbia, and territories of Alaska and Hawaii (USDOL 1953, p. 13).²⁰

FINANCING AND ORGANIZING THE PARTNERSHIP

The Wagner-Peyser Act provided ES grants to states, which they were required to match, to administer state ES systems; and Title III of the Social Security Act provided nonmatching UI grants (and still does) to states to finance the ES system and administer state UI laws.²¹ After 1938, between 85 and 90 percent of the costs for administering ES offices were financed through UI grants. Prior to 1942, between 90 and 95 percent of the entire costs of maintaining the overall state ES office systems were financed by the federal government under the Wagner-Peyser Act and the Social Security Act. Between January 1942 and November 1946, war-time mobilization of civilian labor required federalization of the state ES systems, and the total cost of administering ES offices was paid from federal general revenues. When Congress returned the ES to federal-state administration it waived the state ES matching requirement. The 1947 Labor-

²⁰ For the two FYs, 1938–1939, the board increased its share of the total costs of the ES, from 60 percent, \$14.3 million in FY 1938, to 80 percent, \$25 million in FY 1939 (Haber and Joseph 1939, p. 29).

²¹ Parts of this section are drawn from U.S. Congress (1950).

Federal Security Appropriation Act and subsequent laws (Friedman 1948, p. 17) provided 100 percent federal funding of ES administrative costs until 1950, when the Wagner-Peyser Act was amended to permanently eliminate the matching provision.²²

However, getting the ES and UI programs located in the USDOL to overcome federal and state structural barriers and divide responsibilities to fortify the two programs' partnership proved challenging during the Truman Administration.²³ Ultimately, in August 1949, under Reorganization Plan No. 2, the Bureau of Employment Security with responsibilities for ES and UI was transferred permanently from the Federal Security Agency to USDOL (USDOL 1955, p. 53).

EARMARKING REVENUES FOR EMPLOYMENT SECURITY

Struggles in obtaining adequate appropriations for ES and UI after World War II led to legislative proposals starting in 1949 to earmark FUTA revenues solely for the purposes of employment security—that is, ES and UI. Earmarked funds were thought to be less susceptible to budget manipulations. Not until the Employment Security Administrative Financing Act of 1954 (P.L. 83-567) was the provision enacted to earmark receipts from the FUTA payroll tax for employment security. However, FUTA receipts continued to be deposited in general revenues of the U.S. Treasury and appropriations for ES and UI administration continued to be paid from general revenues. The 1954 law did provide that at the end of each fiscal year, excess tax

²² The cost to states for administering ES offices from 1933 through 1950 in the years when matching was required never exceeded 10 percent (U.S. Congress 1950). Federal law has never prohibited supplementation of funds by states to support the ES system.

²³ In July 1946, the Social Security Board was abolished. Its functions, including UI administration, were transferred to the new Social Security Administration in the FSA. During the presidential campaign of 1948, over President Truman's veto, Congress transferred the ES program from USDOL to the FSA. Thus, the USES and UI were again combined in the Bureau of Employment Security, but not in USDOL.

receipts—revenues over expenditures—were to be credited to the Unemployment Trust Fund (UTF) (Haber and Murray 1966, pp. 404–405).

Since the 1954 amendments, administrative grants for both ES and UI have been financed exclusively from the earmarked payroll tax under FUTA. In the ensuing years, however, USDOL budget requests for ES and UI administrative grants continued to be cut by Congressional appropriators. Thus in 1959, the Eisenhower Administration proposed yet another law change that would require Congress to finance employment security administration directly from the UTF. Amounts equal to FUTA revenues could then be placed in the UTF, from which the grants to states could be appropriated with an adequate balance maintained as a reserve. The president’s budget message for FY 1961 argued that in this way “employment security programs would be financed in essentially the same way as other major social insurance programs” (Federal Reserve Archive 1960).

During the Eisenhower presidency, most of the key architects of the federal and state ES and UI programs remained active in policy making. Based on their experiences, they sought in the late 1950s to strengthen the ES and UI partnership into the future. Congress approved the Eisenhower reform with overwhelming bipartisan support; the Social Security Amendments of 1960 were enacted on September 13.²⁴

Title V of the 1960 amendments, called the Employment Security Administrative Financing Amendments, set up a new federal Employment Security Administration Account (ESAA) within the UTF.²⁵ Under the law, the federal payroll tax paid by employers to the U.S.

²⁴ In contrast to recent partisanship in tax policy, HR 12580 (P.L. 86-778) also raised the federal payroll tax from 3.0 to 3.1 without a change to the allowable 2.7 offset (USDOL 1985, p. 48). The bill sponsored by a Republican administration received 369 House votes to approve, with 236 Democrats voting for it. In the Senate, the bill received 74 votes to approve, with 43 Democrat votes (Social Security Administration 2016).

²⁵ Sections 901(a) and (c) and 903 (c), Social Security Act.

Treasury is deposited in ESAA, and about 20 percent of those receipts today are allotted to the Extended Unemployment Compensation Account (established in 1970). Funds to administer state ES and UI programs are expended directly from ESAA.

Since the amendments of 1960, employer federal payroll tax receipts are deposited to ESAA; a portion of those receipts are retained in ESAA, and ES and UI grants to states are paid directly from ESAA, rather than from the federal general fund (Miller 1997, p. 359). The 1960 amendments instituted a sea change in the fiscal federalism of ES and UI programs. Thereafter, FUTA revenues have not only been earmarked, but they go directly into the UTF and also come out of the UTF as ES and UI grants. Federal ES and UI laws, federal-state grant agreements, and state plans with each state workforce agency set forth conditions for administration of the grants. The 1954 and 1960 revisions to the UTF remain in place, and over time they have safeguarded the framework of the ES-UI partnership.

CHANGES IN THE LABOR FORCE

The role of the ES expanded greatly in the second half of the twentieth century to include serving the disadvantaged, who had little or no previous work experience and difficulty entering the labor market.²⁶ Because more funding for ES was needed to adequately serve the disadvantaged, advocates began to consider additional ES funding sources and arrangements. They argued for the use of monies from federal general revenues to augment ES appropriations and expand service capacity. During this period, the national effort to enact the first large-scale

²⁶ One result of this new target population in the view of some was to diminish employer loyalty in the ES and the potential quality of job seekers that might be referred to job openings.

public job training programs emerged.²⁷ Ruttenberg and Gutchless (1970, p. 73) typified sentiments of some job training advocates, observing that, “Trust fund financing has provided a continuity and stability that was essential to the steady development of the employment service.” They and others argued that funds from the FUTA payroll tax should be used to assist job seekers with prior attachment to the labor force; while additional funds to serve the disadvantaged and others groups should be drawn from federal general revenues to finance some ES administration.

The 1970 Employment Security Amendments (P.L. 97-373) first provided that the ES grants include a “mix” of monies from FUTA and general revenues. Based on USDOL rules to meet statutory requirements, the mix for ES grants is determined by the percentage of employment covered under FUTA. In 1973 the source of funds was 85 percent from FUTA and 15 percent from general revenues. A series of changes in this balance followed. In 1975, the grant mix was set at 86 percent from FUTA and 14 percent from general revenue. In 1976 the proportions were changed to 87 percent and 13 percent, respectively. In 1978, the proportions were adjusted to 92 percent from FUTA and 8 percent from general revenue. Before the summer of 1980, the proportions were again revised to 97 percent from FUTA and 3 percent from general revenues, and since then they have remained unchanged (Lubin 1980, p. 877).

Over the next 30 years, national policy shifted about whether UI and ES services should be delivered jointly or separately at local offices. In 1980, a report by the National Commission on Unemployment Compensation (NCUC) made recommendations to revitalize the ES-UI partnership by enhancing the ES program. The report specified that for ES to serve as the prime

²⁷ The rise of automation as a means of production began to trigger dislocation of workers, whose needs— together with the disadvantaged—prompted the birth of public job training. Under the Manpower Development and Training Act (MDTA) of 1962, ES and UI played vital roles. The state ES screened and referred job seekers to training institutions and UI administered MDTA allowance payments (Wandner, Balducci, and O’Leary 2015).

federal and state labor exchange and provide job search and work test services to UI claimants, the Wagner-Peyser Act ES grant to states needed to be increased. To accomplish essential ES objectives, it was proposed that annual federal grants be sufficient to fund at least four ES staff positions for each 10,000 civilian labor force members in local areas (NCUC 1980, pp. 137, 141). No action by the president or Congress was ever taken on these NCUC policy recommendations.²⁸

ES AND UI AS INTERDEPENDENT PROGRAMS

From FY 1994 through FY 2000, states received supplemental USDOL grants totaling \$825 million to consolidate delivery systems under the One-Stop initiative. Interestingly, one of the federal principles for the states' receipt of the new funding was *integrated services* (Balducci, Johnson, and Gritz 1997, p. 476; Balducci and Pasternak 2001, p. 145).²⁹ The term *integrated service* became a source of policy differences. Reminiscent of the internal debate within USDOL in 1937 but with a different result, some USDOL policymakers in the mid-1990s were concerned that UI would get saddled with large costs for the upkeep of consolidated One-Stop centers, housing multiple program partners. While the same USDOL policymakers previously had been reluctant to sponsor new telephone and Internet UI claims processes, they changed position to avert what was perceived as a grab by One-Stop operators for UI resources. The USDOL began supporting and subsidizing new telephone and Internet technologies, which

²⁸ In the early 1980s, James Rosbrow, executive director, NCUC, told an author of this paper that the report's recommendations were not acted upon because of the publication's timing. It was issued during the 1980 presidential election, and the outcome of that election resulted in a rollback of federal policy making.

²⁹ Supplemental USDOL grants for the development of state One-Stop delivery systems were authorized under the Wagner-Peyser Act, but the source of funds was general revenue. The other One-Stop principles were universality, customer choice, and performance-driven/outcomes based.

resulted in relocating the vast majority of state UI staff out of AJCs and into isolated call and help centers. Currently, most UI staff members are not located in physical AJCs, though states are required to provide access to claims services at these centers (Wandner 2010, pp. 198–199).

With implementation of the One-Stop grant initiative under way, the Clinton administration next sought to enshrine in law this “third-way” One-Stop approach to reform of workforce development programs. Codified in the Workforce Investment Act (WIA) of 1998, this reform brought together the ES, UI, and job training systems into a single One-Stop delivery system, without reapportioning state control of ES and UI programs and local control of job training programs (Balducci and Pasternak 2001, p. 156).

The ES-UI partnership weakened during the WIA era, mostly because of the lack of funding for the Wagner-Peyser Act ES program. It did so despite federal laws establishing new programs requiring ES-UI cooperation to assist increasing numbers of dislocated UI beneficiaries. These included the Worker Profiling and Reemployment Services³⁰ (WPRS) program introduced in 1994 and the Reemployment Services and Eligibility Assessment (RESEA)³² program developed between 2005 and 2015. Over the past four decades, USDOL has

³⁰ Reemployment services are employment services for individuals who have work experience and seek new work.

³² Introduced in FY 2005, the Reemployment and Eligibility Assessment (REA) initiative, retitled as the RESEA, requires UI claimants to report in person to AJCs and receive one-on-one reviews of eligibility for UI, assessing their ability and availability for work, and referrals to reemployment services or training. When the WPRS program was launched in March 1994, an author of this paper coordinated the Employment and Training Administration (ETA) work team that prepared operating guidance to states. The team considered including UI eligibility reviews in the WPRS process, but obtaining funding and setting up the framework would have delayed state implementation. Eligibility reviews were not included in the original WPRS process (USDOL 1994). Later efforts to introduce such reviews lacked policy support, until the launch of the REA initiative. The purposes of WPRS and RESEA are similar—reduced duration and faster job placement. In FY 2015, USDOL merged aspects of the two efforts. Claimants determined most likely to exhaust benefits under state WPRS systems and veterans receiving unemployment benefits are the primary groups directed to RESEA. For a discussion of other aspects of the WPRS and RESEA, see Wandner (2010) and USDOL (2015).

proposed budgets insufficient to provide adequate Wagner-Peyser Act ES grants to states.³¹

Underfunding by Congress has widened the fissure between ES and UI program activities.

Despite these challenges, the union of ES and UI remains intact in federal statutes, and practical operations in the ES-UI partnership are still faithful to the founding principles (USDOL 1955, p. 12), which

- guarantee that impartial services will be delivered by competent state government professionals, free of patronage, or private interests;
- pledge that the prospect of suitable jobs will be found for UI claimants as soon as possible, so that in many cases the payment of benefits will be unnecessary;
- ensure cooperation between job finding and placement, and also between UI claims and benefit payment staff members, in order to satisfy state UI laws requiring that UI beneficiaries must be able and available to work and may be disqualified if they refuse suitable work without good cause (for example, the UI work test to receive benefits);
- agree that when a claimant has refused a referral or a job based upon a referral, the facts must be reported to the claims staff to determine whether a benefit disqualification should be imposed; and
- assure employers that claimants who are required to do so are fulfilling their responsibilities to seek work, and that employers have a reliable means to obtain qualified workers.

³¹ Grants for ES refer to annual base grants, which support staffing and infrastructure of state labor exchange operations under section 6 of the Wagner-Peyser Act. They are distinct from episodic federal grants for reemployment services under the Reemployment Services and Eligibility Assessment (RESEA) initiative.

The WIOA of 2014 retained the WIA's One-Stop concept along with the distribution of authority between federal, state, and local entities. However, WIOA did collapse the WIA categories of core and intensive services into a single category of "career services" without repurposing them. Career services are typically the same as Wagner-Peyser Act ES services. The key differences between ES and WIOA are that ES is under the administrative control of governors' designated state workforce agencies, where resources can be reassigned within states, and services are delivered by merit-based government employees, retaining assurance of impartiality sought by the founders of the ES and UI programs. Grants (derived largely from FUTA) are for administering ES services throughout each state, with distinct responsibilities to UI claimants. Thus, Wagner-Peyser Act ES funds enable governors to align statewide economic development with recruitment and job placement services without destabilizing local WIOA resources in any area. Grants (derived from general revenue) for administering WIOA career services and job training are mostly under the control of local workforce development boards. WIOA services are delivered primarily by private or public employees.

EVIDENCE OF COST-EFFECTIVENESS

Evaluation studies since the 1980s have shown that many dislocated, experienced workers actually only require adequate unemployment benefits and JSA to return to employment (Corson et al. 1989; Jacobson et al. 2004; Johnson et al. 1983). Additionally, random trials testing strategies to renew linkages between ES and UI have estimated shorter unemployment durations, and lower UI benefit payment costs result from closer cooperation (Corson, Long, and Nicholson 1985; O'Leary 2006).

These results mean that conservation of UTF reserves through reduced joblessness can be achieved by providing job finding and placement services and exposing UI claimants to suitable jobs. This is particularly true for younger and dislocated UI claimants. Analyzing data from Washington State, Lachowska, Meral, and Woodbury (2016) find that for dislocated UI claimants the work test reduced time to reemployment by one to two quarters, and increased post-UI job tenure by about two quarters.³²

Other evidence of how a revitalized ES-UI partnership affects the duration of unemployment and job placement nationwide is seen through an examination of several additional USDOL-sponsored studies. A demonstration in Wisconsin (Almandsmith, Adams, and Bos 2006) tested a services regimen that included joint ES-UI staff interviews with UI claimants, JSA, UI eligibility reviews, and staff-assisted job referrals. Using a quasi-experimental methodology, the researchers found that UI durations were shortened by 0.9 of one week, relative to the comparison group of other UI claimants. More evidence of effective ES activities comes from three evaluations of reemployment and eligibility assessments (REA) involving random trials (Benus et al. 2008). In Nevada, the REA led to significantly shorter UI durations and lower benefit amounts where treatment group UI claimants collected 3.13 fewer weeks and \$873 lower total benefit amounts than their peers (Michaelides et al. 2012; Poe-Yamagata et al. 2011).³³

³² The work test is an ES responsibility under the Wagner-Peyser Act, section 7(a)(3)(F). Provision of the work test is not in WIOA. The Middle Class Tax Relief and Job Creation Act of 2012, amended the Social Security Act at section 303(a)(12) to require that UI claimants be able to work, available for work, and actively seeking work.

³³ Some material in this section was derived from Wandner, Balducci, and O'Leary (2015).

INADEQUATE ES FUNDING AND CONSEQUENCES

Because of chronic underfunding of Wagner-Peyser Act ES grants, the types of effective, staff-assisted ES services needed to return the unemployed or underemployed to work are not always available at AJCs.³⁴ Underfunding has occurred in spite of research showing that assessment, JSA, and job finding and placement services can be highly cost-effective ways of reducing joblessness.

Since program year (PY) 1984, Wagner-Peyser Act ES grants to states have remained stagnant or reduced in nominal terms.³⁵ With enactment of the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, there has been a contraction in federal UI program eligibility, manifested in harsher qualifying and continuing eligibility requirements.³⁶ This contraction is the result of federal fiscal policies that promoted reducing the size of the federal government, devolvement of social programs to states, and opposition to federal tax hikes. Accompanying resistance by some states to tax increases in recent years also has resulted in unprecedented reductions in unemployment benefit durations. The potential federal funding of ES-UI programs was further squeezed with the drop in 2011 of the FUTA tax rate from 0.8 percent to 0.6 percent. Likewise, the federal UI wage base, the wage cap per employee used to calculate employers' tax contributions to support the ES-UI programs, has remained at \$7,000, since January 1, 1983. After enactment of the Social Security Amendments of 1939, increases in the federal UI wage base to support these vital programs have occurred only three times, under

³⁴ Over the past few decades, states have cut back on staff-assisted ES service capacity. For example, since 2011 the governor of Iowa has closed 36 offices and reduced state workforce agency staff by 27 percent, which makes it hard "to provide employment services to individual job seekers" (*Des Moines Register* 2017).

³⁵ The Program Year for the Wagner-Peyser Act ES program begins July 1 of the calendar year and ends June 30 of the following year.

³⁶ <https://history.nih.gov/research/downloads/PL97-248.pdf> (accessed February 15, 2017).

Republican administrations, in 1970 (P.L. 91-373), 1976 (P.L. 94-566), and 1982 (P. L. 97248).³⁷

The federal contraction of UI entitlements and reduction in funds for ES services occurred at a moment of enormous technological advancements. This leap in technology enabled states to shift to high volume mainframe and distributed computer processing and Internet services without workload reductions. Sometimes, particularly in rural areas, this gave a false impression that access through computer-assisted services always resulted in effective service interventions (Dunham et al. 2005). With federal budget constraints and the rampant use of technology-based self-services, there has been precipitous erosion in staff-assisted ES job finding and placement services. Since then, regular UI average duration and the regular UI exhaustion rate have been trending upward, suggesting a possible cause and effect.

From 1993 until the first decade of the twenty-first century, the WPRS program required states, as an unfunded mandate, to provide reemployment services to additional UI claimants likely to exhaust benefits. As a consequence, ES services in states were widely underfunded and WPRS claimants underserved.³⁸ Advancements in self-service through virtual tools, reductions in ES grants, and a conflicted federal WPRS policy led many states in the 1990s to abandon most if not all staff-assisted ES job referrals and placement services.

³⁷ In 1939, two federal laws were enacted that affect the ES-UI partnership. P.L. 76-1, untitled, transferred Title IX of the Social Security Act to the Internal Revenue Code. The Social Security Amendments (P.L. 76-379), limited the tax base under FUTA to the first \$3,000 of a covered worker's earnings (USDOL 1986, p. 43).

³⁸ An author of this study and others at USDOL began in 1997 drafting internal papers arguing for increases in Wagner-Peyser Act ES funds to serve dislocated UI claimants. Separate approvals were required from ETA, other offices in the USDOL, the Office of Management and Budget (OMB), and Congress. It took three years to gain concurrences. For PYs 2001–2005, Congress added \$35 million to the Wagner-Peyser Act ES appropriation to serve WPRS UI claimants, but these funds were inadequate. Subsequently, the George W. Bush Administration abandoned supplementation and cut Wagner-Peyser Act ES grant funds. In 2009, the Obama Administration, under the American Recovery and Reinvestment Act, achieved a one-time increase in Wagner-Peyser Act ES grants of \$400 million, available through PY 2010, which included \$250 million targeted for reemployment services to UI claimants.

A structural underfunding of the ES program has occurred in recent decades, meaning that it cannot serve the full array of job seekers that could benefit from reemployment services. And the ES program has received relatively fewer resources from the Congress than public job training programs, which have acquired more political attention. Since 1962 there have been five major federal job training laws, including WIOA, each with companion changes to state and local delivery structures.³⁹ Each incarnation of public job training has been funded from general revenues of the federal government by discretionary Congressional appropriations. Public job training is neither an entitlement, nor does it have a statutory funding mechanism.

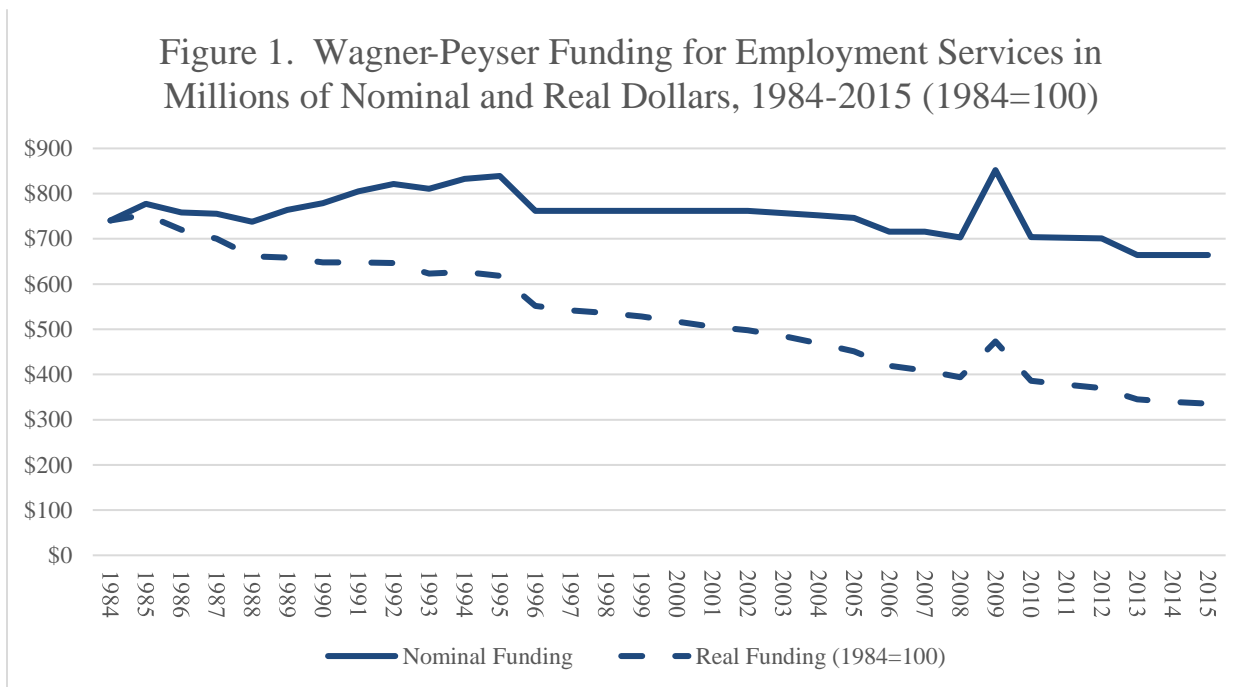
On the other hand, most developed industrial nations provide a free public employment service as a right to all citizens. Indeed, these developed nations and many middle-income nations, are signatories to the 1948 International Labor Organization (ILO) Convention 88 on public employment services (ILO 1948). Although the United States is not a signatory of ILO Convention 88, it has respected the principle of the convention that all nations “shall maintain or ensure the maintenance of a free public employment service (ILO 1948, article 1).” The idea is that labor force members should have a right to free labor market information and job matching services as a means to social participation. As President Eisenhower said, “(S)tate employment security offices are important for a smoothly operating free labor market in a growing economy” (Federal Reserve Archive 1960). Through the FUTA payroll tax, Wagner-Peyser Act ES services have a statutory funding mechanism to ensure Americans the entitlement to a free public employment service. Political action should be taken to ensure adequate FUTA funding for the ES, and remove it from the vicissitudes of Congressional appropriations. In the American society

³⁹ O’Leary, Straits, and Wandner (2004) review the first four federal job training laws.

where work is the avenue to self-sufficiency, a free and open public labor exchange is a right of all job seekers.

Because Wagner-Peyser Act ES grant funds to states since PY 1984 have declined in nominal terms, their real value through PY 2015 has dropped by more than half (Figure 1). For 2015, funding of \$1.47 billion would have maintained the 1984 real level of spending.⁴⁰ Workers and employers should be more aware of the role ES contributes to the smooth functioning of the labor market and to the integrity of the UI program. Some states have taken limited measures to make up for portions of these ES grant shortfalls by augmenting federal funding through special assessments or by tapping UI funds. Thirty states as of 2015 provided supplementary ES funding (USDOL 2016a, Table 2-17, pp. 2-31 to 2-32). Additionally, based on the annual National Association of State Workforce Agency (NASWA) survey of state workforce agencies, state supplementary spending on ES totaled more than \$150 million (NASWA 2016). This is compelling evidence that state workforce agency administrators value ES programs for their customers.

⁴⁰ The implicit price deflator value for 2015 was 197.97 with the base year 1984, and the nominal 1984 level of funding for Wagner-Peyser Act programs was \$740 million.



Sources: BEA (2015), USDOL (2014, 2015a, 2015b).

OPPORTUNITY FOR ES-UI PARTNERSHIP REVITALIZATION

Over the years, the ES-UI partnership has ebbed and flowed. Historically about 40 percent of the ES registrants for services have been UI claimants. In the Great Recession, the highest number of ES registrants in any year was 22,447,124 in PY 2009, and of those, 10,712,573 were UI claimants, totaling 47.7 percent of all registered ES job seekers (USDOL 2009).

Workforce changes over several decades and new work arrangements in today's so-called gig labor market have resulted in more workers being at risk for joblessness. Currently, fewer than one in three unemployed workers receive unemployment benefits, and a record high 38 percent of workers exhaust benefits. After the Great Recession, nine states (Arkansas, Florida, Georgia, Illinois, Kansas, Michigan, Missouri, North Carolina, and South Carolina)—mostly as

a result of debt due to inadequate benefit financing—reduced their maximum unemployment benefit durations to less than 26 weeks, ranging from 12 weeks to 25 weeks.⁴¹ The number of weeks available in four of those states (Georgia, Florida, Kansas, and North Carolina) is based on a sliding scale governed by the states’ unemployment rates (the White House 2016).

The decisions by some states to reduce UI benefit durations have adverse effects on both claimants and job seekers that have exhausted unemployment benefits. Reductions in UI receipt by unemployed workers will not reduce the number of job seekers who need ES services. Business downturns or dislocations will cause many claimants in states with reduced durations of benefits to exhaust, but still they likely will continue to be job seekers. These job seekers—that is, UI exhaustees—will still need an array of job finding and placement services. Shortened maximum durations make provision of early ES services even more important. For example, in PY 2014, UI claimants accounted for 37.3 percent of all job seekers registered with ES—a 10 percentage point decline from PY 2009 (USDOL 2014). While much of this decline may be attributed to improved economic conditions, should additional states reduce their maximum duration of benefits, the percentage gap between UI claimants and ES job seekers may widen. However, the necessity for employment services to job seekers that have exhausted unemployment benefits will remain.

In June 2016, the Center for American Progress (CAP), the National Employment Law Project (NELP), and the Center on Poverty and Inequality (CPI) of the Georgetown University Law Center proposed to improve unemployment protections for workers and enhance the ES-UI

⁴¹ In 2013, Illinois resumed a 26-week maximum UI duration.

partnership. They called for a \$1 billion increase in Wagner-Peyser Act ES grants and a \$535 million increase in RESEA above the 2017 presidential budget request (West et al. 2016, pp. 20–21).

If the Trump Administration is successful in stimulating aggregate demand, then domestic labor demand is also likely to increase. Many businesses with job openings will require some staff-assisted ES recruitment services. This possible surge in labor demand is an ideal time for policymakers to strengthen the ES-UI partnership by acting upon the CAP-NELP-CPI recommendations.

POLICY OPTIONS FOR IMPROVING ES-UI PARTNERSHIP

Acknowledging the recent accomplishments of USDOL to improve the public workforce system, we offer four policy considerations to revitalize the ES-UI partnership.

Increase Annual Wagner-Peyser Act ES Grants to States

In FY 1981, regular Wagner-Peyser Act ES grants totaled \$781.4 million. That year ES grants served 16.5 million job seekers (USDOL 1982, pp. 48–49). Had ES received only an inflation-adjusted increase in annual funds in the ensuing years, the amount would have been \$1.47 billion in FY 2015 instead of the \$664 million appropriated by Congress. We support the funding increases proposed by CAP-NELP-CPI.

Jacobson (2009, p. 25), in a report issued by the Brookings Institution, estimates a cost of \$383 per UI claimant to institute a call-in notification and conduct JSA services. Calculating for annual inflation, the cost rises to \$430 per UI claimant in 2016. From historic usage, \$430 seems a reliable estimate for the average cost per additional UI claimant to receive staff-assisted

assessment and job search services.⁴² Using the \$430 amount, the proposed \$1 billion in added Wagner-Peyser Act ES grants could provide job search activities to an added 2.3 million UI claimants (or the long-term jobless who exhaust unemployment benefits). In FY 2015, for instance, only 16 percent of UI claimants were scheduled for RES or RESEA eligibility and job search services (USDOL 2016b, p. 37). Therefore, using PY 2014 national ES data, 5,411,656 UI claimants were registered with ES, and of those, 1,845,036 received job search activities; the added ES funds of \$1 billion could have increased the receipt of job search activities for UI claimants from 34.1 percent to 77 percent.⁴³

Furthermore, amendments to the Wagner-Peyser Act in WIOA expanded ES assistance to UI claimants, added work test responsibilities to include making eligibility assessments, and broadened its referrals and application assistance to other training and employment opportunities.⁴⁶ Logically, additional ES responsibilities should give rise to increases in annual Wagner-Peyser Act ES grants to states. Thus far, increases in federal ES grants to states have not occurred.

Raise and Index the FUTA Taxable Wage Base and Make ES Grants Budget Mandatory

A vibrant and free public employment service is an American right. Restore the statutory funding capacity of the Wagner-Peyser Act ES program by raising and indexing the FUTA taxable wage base. Move the Congressional allocation derived from funds in ESAA for state ES grants from the discretionary to the mandatory side of the federal budget.

⁴² The ES provides job finding and placement services to all job seekers who ask for them. In PY 2014, the cost per individual for ES was \$45.74. This rate included individuals receiving self-service through virtual tools and those receiving staff-assisted ES services (USDOL 2016b, p. 53). The cost per individual is too low to help many job seekers who need person-to-person counseling and JSA.

⁴³ The actual 1,845,036 UI claimants in receipt of job search activities added to an estimated 2,325,000 UI claimants in receipt of job search activities totals 4,170,036 UI claimants. ⁴⁶ Sections 7(a)(3)(F) and (G), Wagner-Peyser Act.

In order to secure additional Wagner-Peyser Act ES financing, the FUTA wage base could be tied to one-third of the Social Security taxable wage base or set equal to the average annual weekly wage in UI covered employment. Either rule would secure the foundation for Wagner-Peyser Act ES grant financing and help insulate it from the politics of the budgetary of request and appropriation processes.

Create a Contingency Fund for Wagner-Peyser Act ES program

Starting in FY 1950, the federal budget for state UI grants has contained a contingency fund to meet additional state workload expenditures. This fund was designed to encounter specified costs above the budgetary levels for the number of UI claims filed and claims paid (USDOL 1957, p. 6). The USDOL should create a companion ES contingency fund so that as UI workloads climb, so do ES funds under the Wagner-Peyser Act.

Establishing an ES contingency fund will ensure that as state UI workloads go up, funds above budgetary levels for Wagner-Peyser Act ES services would rise proportionally. These additional ES funds would be provided to serve added UI claimants and provide to them cost effective, staff-assisted ES job finding and placement services. Also, such funds could be used to administer increased work test activities and referrals to appropriate training. A federal-state work group should be assembled to design and test an ES contingency model to determine its effectiveness and exportability.

Increase Uniformity of State UI Provisions

Reforms of the Social Security Act and FUTA and state UI financing rules will be more successful if UI eligibility provisions that are truly national in scope—such as not disqualifying individuals for benefits who leave work to care for immediate family members who are ill or disabled, or to accompany spouses who are relocating—and program alternatives—such as short-

time compensation and self-employment assistance—are made federal conformity requirements where states are compelled to enact companion laws.⁴⁴ This will ensure that conditions for receipt of benefits are uniform state-to-state, and lessen the advantage of one state over another as a cost of doing business. Likewise, such federal policy mandates will advance national economic security outcomes, increase reciprocity, strengthen the ES and UI partnership as an economic stabilizer, and expand labor mobility and the equal treatment of workers.

SUMMING UP

The ES-UI partnership is rooted in permanent authorizing statutes, an identical fund source, common rules for state administration, and interdependent practices to guard against improper payments and expose claimants to suitable job openings. This partnership is central to the success of the public workforce system. Over the past several decades, USDOL has neglected strengthening the UI-ES partnership, despite research evidence that demonstrates its value to reducing unemployment durations. During recent recessions, federal policies have increased emergency unemployment benefits and job training but by and large ignored long-term underfunding of Wagner-Peyser Act ES grants. As a result, Congress has been inattentive to the inadequacy of ES finances. Correspondingly, in many instances state governors and some advocacy groups have overlooked their roles in promoting the UI-ES partnership and increasing ES grants.

In this study, we explored the origin and objectives of the ES-UI partnership. We reviewed the actions in the early years by the ES and UI framers to forge an interdependent

⁴⁴ The National Governors Association’s principles of state-federal relations endorse federal action for problems that are truly national in scope (National Governors Association 2017).

relationship between the two programs. In the beginning, creative financing and strict rules for professionalism were required to properly launch employment security programs. A statutory system for cooperation and financing was set by 1960, but it has atrophied—along with the ES and UI partnership—mostly because of inattention and underfunding of the ES program. We reviewed recent research that demonstrates the effectiveness of employment services and the reliance of the ES and UI programs on each other to achieve social insurance principles. We described how amendments to the Wagner-Peyser Act in WIOA broadened ES activities, and we proposed a path to revitalizing the long-standing ES-UI partnership.

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