Policy Issues: An Overview

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Chapter 1 (pp. 1-49) in:
Unemployment Insurance in the United States: Analysis of Policy Issues
Christopher J. O’Leary, and Stephen A. Wandner, eds.
Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 1997
DOI: 10.17848/9780585338408.ch1

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The federal-state program of unemployment insurance (UI) is well established among economic institutions in the United States. It has an undeniable influence throughout the economy, affecting personal incomes, employer taxes, federal-state relations, and interstate competition for industrial production and employment.

The UI program serves a variety of functions that help frame employment relations between Americans. Over the nearly sixty years since the program’s inception, these functions have come to be accepted and relied upon by both workers and employers.

UI partially replaces lost income for individual workers who are involuntarily unemployed, and, in the aggregate, it helps to maintain purchasing power during economic downturns. It reduces the dispersal of skilled workers when employers impose temporary layoffs and helps prevent the breakdown of general labor standards during such periods. Some features unique to the UI system in the United States are designed to encourage employers to stabilize employment levels.

During the twentieth century, the existence of a reliable system of unemployment compensation has become a hallmark of a developed, modern industrial economy. Rapidly growing middle-income countries, from central Europe and sub-Saharan Africa to southeastern Asia, are experiencing urbanization of their peoples and are seeking systems
for insuring incomes. There is a recognition that workers in an industrial economy are separated from the subsistence guaranteed by the land in an agrarian society. When designing a safety net for workers, these emerging nations are faced with two broadly differing strategies concerning UI.¹

The UI approach popular in Europe emphasizes income replacement without much attention to return to work or to stabilizing employment. The American UI system presents a distinct alternative, which is custom designed to operate in a competitive market economy. The system in the United States emphasizes individual responsibility, while the European system views unemployment compensation as a social obligation.

At the core of most contentious issues in the federal-state UI system in the United States is the struggle between social generosity and individual responsibility. These competing interests must be weighed to determine matters such as the scope of coverage, the requirements for benefit eligibility, the appropriate level and duration of benefits, and the distribution of the financing burden.

Social attitudes about the unemployed as workers and income providers shape the public view of unemployment. Perceptions about employers as business operators and job providers influence how the public sees employer responsibilities for workers. Also critical to resolving UI issues are public attitudes regarding the proper role of government in dealing with the problem of unemployment.

The diverse issues generated by conflicting public opinions are difficult to sort out neatly. Yet, this chapter attempts to make a brief exposition of some of these attitudes and of the broader and more fundamental controversies they engender so as to help illuminate the later discussions of specific program issues. In the next section, the genesis of the UI program and the controversies surrounding it are examined. This analysis begins with a brief review of the historical context of UI and is followed by a discussion of public attitudes toward unemployment and about UI. The third section of this chapter, which considers UI in the larger context of economic security, includes a discussion of the distinctions between UI and welfare programs, UI as part of the whole social safety net, and the role of UI in the overall economy. Conflicting and shifting viewpoints about the causes of unemployment and the character of the unemployed then lead to an
overview of the basic controversy concerning the UI program's effects on the incentive to work. Fifth, the subjective element of an individual's unemployment is considered as the basis for questions about fairness and efficiency in administration and about possible fraud and abuse of the system. The sixth section discusses the controversy arising from employers and workers pressed to advance their particular economic interests in regard to issues of UI taxation and benefit levels. The conflict inherent in the federal-state relationship on which the UI system is built is subsequently reviewed as a source of dispute in the program. The chapter concludes with reflection on whether and how knowledge about the working of UI is used to improve the system.

**Genesis of the Program and Controversy**

*Historical Context of Controversy*

The federal government's adoption of a major, active role in social planning during the Great Depression provoked widespread public controversy because that move departed from the traditional *laissez-faire* approach of government. Prior to the 1930s, unemployment was not regarded as much more than a temporary and occasional problem, an inevitable seasonal or cyclical malady of industrial society. Once business and employment recovered, public concern about unemployment faded. Workers who experienced much unemployment were often seen as responsible for their own predicament. They were viewed as either not industrious enough to hold steady jobs or fundamentally flawed in their character. In cases where job and wage loss produced temporary family deprivation, local privately funded welfare agencies were regarded as the appropriate sources of assistance. In some areas, public unemployment relief was provided by local government.2

Public UI proposals were advanced in a number of states before 1930, but these initiatives were not broadly accepted given prevailing attitudes. The thought of federal government intervention to deal with unemployment was an even more remote idea and viewed as probably unconstitutional. Most employers did not see provision for the unemployed as a responsibility of business. The few who did thought that
unemployment benefit plans should be provided by employers on a private, voluntary basis.

The reality of mass unemployment during the depression of the 1930s made clear that personal deficiency was not the only cause of the problem. As joblessness reached into the homes of executives, white-collar workers, and skilled mechanics—people who heretofore had been untouched by unemployment—the realization grew that the industrious and efficient worker as well as the marginal, unstable, lazy worker could be affected. Moreover, the problem was not of brief duration; unemployment persisted. Personal economic hardship among the jobless became widespread. Efforts to ease these difficulties overwhelmed private welfare resources and local government relief. Resistance to large-scale government assistance for the unemployed could not long withstand the pressures exerted by the massive needs of so many over so many years.

Old attitudes began to give way, though not willingly or universally. The exposure of millions of workers and their families to the indignity of applying for and accepting relief shifted opinions sufficiently to broaden the support for unemployment benefits provided on an orderly, prefunded, social insurance basis. Employer organizations continued to resist the coming of UI, but with the continuation of the depression, it could no longer be denied.

The federal-state unemployment compensation program was authorized as part of the Social Security Act enacted August 14, 1935. As a result of tax offset inducements contained in the companion Federal Unemployment Tax Act, by July 1937, in all states plus Alaska, Hawaii, and the District of Columbia, legislation had been passed to create UI programs. “The constitutionality of the state and federal laws was challenged in several states as soon as [UI] taxes became payable on employment after January 1, 1936. The U.S. Supreme Court upheld the constitutionality of the New York law in November 1936, and that of the Social Security Act and the Alabama Unemployment Compensation Act in May 1937” (Rosbrow 1986, p. 7). In writing the majority opinion, Justice Benjamin Cardozo asserted that it was not a lack of compassion for the unemployed, but rather a reluctance to competitively disadvantage native industries that discouraged states from independently establishing UI systems before 1935.
While the depression altered general attitudes enough to make the federal-state UI system possible, the opposing points of view did not disappear. Today, UI is widely accepted as a permanent public program. Millions of Americans, however, still find it difficult to accommodate themselves philosophically to the idea that unemployed workers should be allowed to receive benefits as a matter of right even if they do not appear to need them. Unemployment is recognized as a continuing problem, although it is more acute during dips in the business cycle than at other times. Most unemployment is viewed as the consequence of impersonal economic forces, but during nonrecession periods, the belief that unemployment is the fault of the worker usually resurfaces. Thus, this classical view of unemployment lives on within the populace and forms a significant basis for continued controversy about many UI aspects and for resistance to the program's expansion and improvement.

In the 1980s and particularly in the 1990s, this perspective on unemployment has been partially offset by a growing public awareness of the impact of permanent worker dislocation, which results from increasingly competitive markets at home and abroad and from the impacts of rapid technological change. The widespread potential for worker dislocation has caused the public to be more concerned about unemployment, even in nonrecessionary times.3

Public Attitudes toward Unemployment in a Market Economy

As noted, the general view prior to the 1930s was that unemployment was primarily the result of the individual's own deficiency. The experience of the Great Depression shook this position, but its hold on the public mind has remained a strong force, making difficult nearly every effort to extend and improve the UI program.

One expression of this view appeared in the Wall Street Journal in 1914:

Let any man ask himself how often has he seen really industrious workmen out of employment for any length of time, except by their own choice in a labor dispute? The man who wants work can get it, and can soon establish a character that will get him better work (Wall Street Journal, March 5, 1914).
In her classic 1930 analysis of case studies of unemployed persons, Clinch Calkins summed up the earlier attitudes as follows:

There are several widely held ideas about unemployment. . . . One of them is that unemployment comes only in hard times. . . . A second presumption is that under unemployment only those who have been too thriftless to save suffer. And still a third, the most pervasive of all, is that if a man really wants to find work, he can find it (Calkins 1930, pp. 20-21).

A quarter of a century after the federal-state UI system had been established, a sample survey of urban Ohio households gave evidence that a large proportion of Americans still held to the idea that those who truly want work can always find a job. When asked “whose fault is it when people become unemployed?” 37 percent of employees, 38 percent of the self-employed, and 58 percent of employers interviewed put the blame on the unemployed themselves (Ohio State University Research Foundation 1963). Among employees, those in professional occupations were most likely to respond this way (48 percent). Professionals were also least likely to experience unemployment. Among unskilled workers, the proportion blaming workers for their own unemployment was much less (23 percent). The higher respondents’ educational attainment, the more likely they were to blame a jobless worker for being unemployed and, as noted by the survey report:

The people with the greater amounts of formal education, presumably the most informed people, are those who most likely have been exposed to the ideas of economics, including the widely-held notion of involuntary unemployment. Yet this seems to make little difference regarding their beliefs about the reasons for unemployment. It must be, therefore, that this attitude is the manifestation of a more-or-less deeply held belief that is not susceptible to alteration or modification merely through exposure to the thinking and opinions of those generally regarded as “experts” (Ohio State University Research Foundation 1963, p. 33).

Adams (1971, p. 22) reviewed a 1965 Gallup Poll conducted for the Washington Post in which 75 percent of a national sample responded yes when asked, “Do you think many people collect unemployment benefits even though they could find work?” (Washington Post, September 16, 1965). Respondents were more likely to answer in the affirmative if they had higher incomes and more education.
Since the 1960s, there have not been any surveys specifically measuring the extent of public belief that unemployment is the fault of the individual. Views expressed on occasion in the news media or by business and political leaders give evidence that this attitude still holds to a significant and influential degree. These opinions may be heard as complaints that positions go unfilled while jobless workers crowd the UI rolls.4

Recognition that the unemployed may not always match the requirements of the vacant jobs, or that their location may be wrong, or that employers seeking workers may not always be willing to offer reasonable wages sometimes tempers such a blanket indictment. Citing case studies of unemployed white collar workers, a March 1993 cover story in Fortune magazine said that “while the economy is growing steadily again, more than nine million Americans remain jobless, victims of changes they cannot control” (Erdman 1993, pp. 40-49).

Regardless of who is to blame for unemployment, the American public regards it as a serious national problem. When asked in 1994 by Princeton Survey Research Associates for Newsweek magazine, “How concerned are you about the effects of unemployment and a lack of good-paying jobs?” 92 percent of the national sample of 742 adults said that they were either somewhat or very concerned.

In a series of national surveys conducted between 1988 and 1995 by the Hart and Teeter Research Companies for NBC News and the Wall Street Journal, registered voters were asked, “Which of the following list of economic issues facing the country do you feel is the most important right now: inflation, unemployment, interest rates, the Federal budget deficit, Federal taxes, or the U.S. trade deficit?”5 The survey was conducted more than a dozen times, at approximately six-month intervals. Unemployment and the federal budget deficit always topped the list of most important economic issues. In June 1988, unemployment was picked by 28 percent, while 34 percent said the deficit; by January 1992, as unemployment had risen, 53 percent said unemployment, while 16 percent said the deficit; and by January 1995, as unemployment fell, the responses were nearly identical to those in June 1988. Public sentiment expressed in these survey results clearly reflects the competing pressures on UI policy makers. Notably, survey respondents indicated the third most pressing economic issue to be federal taxes.
Public Attitudes toward Unemployment Insurance

Many Americans have viewed UI not as a social insurance program but more like welfare and other public assistance programs. As such, these individuals consider UI as running counter to such historic values as individual and local self-reliance and a free market economy. Writing in the mid-1950s, the historian Max Lerner noted in his study *America As Civilization* that the process of social reform and increased assumption by the state of responsibility for certain needs of the people had been going on since the start of the century, and that the process was opposed throughout by various interest groups, in part by invoking those historic values. These public programs developed with great difficulty, much reluctance, and almost grudgingly. Lerner wrote that Americans have responded piecemeal and in irregular fashion to the need for workmen's compensation, unemployment benefits, old-age insurance, subsidized low-cost housing (etc.) . . . what has emerged in each area of welfare is the acceptance of the principle of responsibility but with the least challenge to private enterprise, the least burden on the tax structure, and the greatest reliance on the voluntary principle. The broad formula has been for the government to set a floor below which security and welfare cannot fall, to use government funds for the more claimant forms of social insurance but to let the others go, to give the states the widest possible discretion, to steer away from centralized authority and administration...to put the burden of expanding the programs upon continued popular pressures (Lerner 1957, p. 131).

In this passage, Lerner identified the heart of much of the basic UI controversy. The program was designed to minimize any disruption to the private free market system. Political pressures work toward keeping it contained. Employers have sought to keep their responsibility for financing unemployment compensation narrow and limited. Through its experience-rated UI tax structure, the program seeks to allocate responsibility for benefit charges among those businesses giving rise to those charges; this tax structure thereby also gives employers an incentive to avoid layoffs and to stabilize employment. Experience rating also results in constant pressure from employers to keep compensation
levels at a low level of protection, so that benefit charges and UI taxes can be held to a minimum.

From the beginning, the states have enjoyed wide discretion in setting specific benefit and tax provisions of their UI laws. Furthermore, there has been resistance to any attempts to set federal minimum standards or to any strengthening of federal authority in the program. Expansion of the program has usually occurred only when organized labor has been strong enough, or when unemployment has been widespread enough, to bring sufficient pressure on the state legislatures or on Congress to act.

Despite resistance, government entitlement programs have multiplied and expanded over the years. UI evolved into a broader program than at first deemed appropriate or affordable when it was initiated during the Great Depression. The system now covers nearly all wage and salary workers and provides much longer periods of protection than it did originally.

Adams (1971) provided a comprehensive review of American sentiments in *Public Attitudes Toward Unemployment Insurance*. In summarizing evidence of declining American support for UI from the 1930s through the 1960s, as preserved in the archives of the Social Security Administration by the Roper Center, Adams wrote the following:

> The Social Security Act programs were deeply rooted in the Great Depression experience. The effects of that experience on public attitudes have diminished as time has passed and memories have dimmed. . . . Those people who were 10 years old or over in 1930 and therefore may be presumed to have personal memories of the Great Depression years constituted 50 percent of the population over 19 years of age in 1965 . . . 38 percent by 1970 . . . and 22 percent by 1980. . . . The impact of the Great Depression on attitudes toward the unemployed and unemployment insurance will be transmitted indirectly, if at all, to succeeding generations, and this fact may be expected to have substantial influence on the program in the future (Adams 1971, pp. 17-18).

By the 1980s, for many Americans, the expansion of social programs and government regulation of economic activity had gone too far. This reaction lent support to attempts at limiting the scope of some programs, to reducing their size, and to restoring the vigor of free mar-
ket principles throughout the economy. In the mid-1990s, the exigencies of persistent federal budget deficits further curtailed government largess and involvement.

These trends have affected the UI program as well, influencing the movement toward more restricted eligibility, more punitive disqualifications among beneficiaries, and more limited levels and duration of benefits. Nonetheless, nationwide surveys of public sentiment indicate broad-based support for the present system of income security for workers. When asked in 1987 by an ABC News/Washington Post survey if spending on UI should be increased, decreased, or kept about the same, 86 percent of a national sample of 1,505 adults said that spending should be increased or kept the same. When the National Opinion Research Center asked the same question in 1990, 75 percent of 1,217 adult respondents in a national survey said that spending on UI should be increased or kept the same. In January 1995, when the Los Angeles Times asked a national sample of 1,353 adults, “Do you think government should cut back spending on unemployment insurance programs?” only 30 percent answered yes.

In the 1990s, the reality of increased worker dislocation, greater public awareness of this issue, and the need to provide early, systematic reemployment assistance resulted in a policy response that began directing the UI system more toward reemployment. The 1993 Worker Profiling and Re-employment Services (WPRS) system mandates nationwide an additional UI eligibility requirement of early active reemployment efforts for beneficiaries who are identified as most likely to exhaust their entitlement. The emphasis on reemployment—and economic development—further resulted in legislation allowing states the option of using UI trust fund money to help “profiled” beneficiaries become self employed; the enabling legislation was included in the North American Free Trade Agreement (NAFTA), which was signed into law by President Clinton in November 1993. The UI program has also adopted an ongoing, active approach toward the prevention of unemployment; this strategy is based on state “work sharing” programs. Work sharing schemes have been included in the UI provisions of 18 states since 1978, when California enacted the first work sharing program in the U.S.

The ebb and flow of prevalent views about the role of government in the economy and society will no doubt continue indefinitely, influ-
enced largely by how economic conditions affect public attitudes generally. That ebb and flow will ensure the continuation of controversy surrounding UI as it reflects the tensions between social equity and economic efficiency.

Unemployment Insurance and Economic Security

The Welfare-Insurance Dichotomy

The widespread hardship endured in the 1930s made large public relief programs politically acceptable. At that time, the typical worker struggled alone to sustain a family, which tended to be larger than is the average family late in the twentieth century. Multiple-earner households were comparatively rare in the 1930s. Loss of work by the breadwinner put families into a crisis situation very quickly. The depression spread penury like a plague among families that heretofore had escaped serious unemployment. Needy individuals and families who accepted relief suffered social indignity and loss of self-respect. Consequently, the concept of unemployment benefits provided on an insurance basis had considerable appeal.  

The idea that contributions to a reserve fund, based on earnings, could provide workers surety against the risk of total wage loss from unemployment came to be regarded as far superior to reliance on charity or on relief, which required a painful public admission of poverty. Rights to UI benefits were earned through working; the question of demonstrated individual need was irrelevant. The insurance concept became and remains important to workers.

UI is social insurance, not private insurance. The major differences between the two are summarized in table 1.1. Indeed, many of the features of UI that make it social insurance also mean that its existence would be impossible under private arrangements. Without government mandate, nothing like UI as we know it would be available: because of a type of market failure, private markets would not provide what society requires as generalized insurance against unemployment for workers.
The UI program aims to provide protection against a risk so widespread that it is social in scope. Without some organized system of relief against unemployment, massive problems of social dependency could result. UI benefits provide a minimum floor of protection that prevents individuals from becoming a social burden and that collectively helps to minimize fluctuations in aggregate consumer spending. This *public good* would not be available without government-mandated participation in the system. If the UI program were voluntary, it would collapse very quickly. Workers with a low risk of job separation would realize that they could save money on premium payments by
breaking away and forming their own low-risk pool. This would eventually result in those with a high risk of unemployment facing premiums so large that they would go uninsured, leaving them with public or private social assistance as their only means of income security.¹²

Social insurance embodies both the incentive aspects found in private insurance contracts and the eligibility features required by considerations of social adequacy. Private insurance contracts provide payment for losses due to occurrence of the insured risk, with the compensation amount dependent on premiums paid. Social insurance bases amounts of payments on some estimation of presumed need, so that compensation is not always directly related to contributions, and eligibility is not always based on the ability to avoid the risk. UI places a ceiling on how far benefits can go in compensating for wage loss, thereby reducing the fraction of earnings replaced for higher-wage earners. Some state weekly benefit formulas weight the benefit-wage replacement ratio to favor low-wage earners. Some states provide allowances for dependents. These provisions reflect the social welfare intent of the program to concentrate benefits more on those who are presumed to need them more. Although its insurance character is well established and supported, the extent to which the program should reflect welfare objectives has been a source of some controversy.

There is a handful of features that objectively distinguish UI from welfare. When characterizing social insurance, Rejda stated five clear distinctions from social welfare, which apply to UI and can be summarized as follows.

1. UI benefit levels are predictable since they are based on explicit formulae that apply to applicants uniformly, while in relief programs the benefit is dependent on the degree of need demonstrated.
2. Financing is done out of specifically earmarked taxes, while public assistance is paid from general revenues.
3. All those covered by UI are participants in the program, with only a fraction ever drawing benefits, while only those who apply for and receive benefits are participants in social welfare programs.
4. No stigma attaches to the receipt of a UI payment, “which provides compensation for wage loss as a matter of right with dignity and dispatch.”¹³
5. The UI program presumes need due to the economic loss resulting from unemployment, while general relief requires demonstration of need, often including the shedding of personal assets.

The last of the preceding differences probably has contributed most to the UI controversy. The welfare aspects of UI have been drawn into question because of the changing perception of the economic position of American workers and their families. The circumstances of the average worker today are far different from those of the average worker more than a half century ago. By and large, the public in the 1990s is less likely to regard unemployment with the same sense of urgency or to see the unemployed so generally in such desperate straits as was the case in the 1930s. Need is not so widely presumed to be as universal or as evenly felt among various segments of the unemployed.

In the Great Depression, the real extent of the unemployment problem was not precisely known. Estimates hovered in the range of 15 to 25 percent of the labor force being out of work (Levitan, Mangum and Marshall 1981). Reliable national income accounting and labor force estimation practices were undeveloped. Since that time, information about the operation of the economy has steadily improved, and, for better or worse, has guided national economic policy. The result of this evolution, together with other institutional reforms in the social, legal, banking, and trade sectors, has been that none of the ten economic recessions since 1946 has even approached the widespread collapse of economic activity suffered in the 1930s (Moore 1980; U.S. Department of Commerce 1995).

This relatively stable labor market has greatly reduced the personal fear of unemployment. For the large majority of Americans, the Great Depression is an item in history rather than a personal memory. Most have never known serious unemployment or felt its consequences close at hand. Many do not identify with the unemployed. On the other hand, increasing worker dislocation over the past twenty years has spread the potential for permanent job loss, bringing the uncertainty of employment to white-collar workers, where it previously belonged primarily to blue-collar workers.

Workers today also enjoy a much improved standard of living. The multiple-earner household is more the rule than the exception, giving many families a broader income base and less vulnerability to the
effects of job loss by one family member. Unemployment for any lengthy period can still produce heavy financial strains, even disaster, as many households have built their higher living standards on a base of substantial indebtedness as well as on increased income.

There has been some pressure for better protection under the program for the unemployed who clearly are in need. Some UI critics see the program largely as protection for the middle-class worker: many of the poor, low-wage, or marginal workers who are unemployed are either excluded or receive very inadequate benefits. It has been suggested that, to broaden access to the program, eligibility requirements be relaxed so that marginally attached workers may qualify for some UI benefits. Sharply increased minimum weekly benefit amounts could be justified on the ground that existing low minimums inadequately support even a subsistence standard of living. Others argue that benefit levels are sufficient, but that benefit durations are inadequate. Many industrialized nations supplement UI benefits with unemployment assistance, which provides means tested income support for people who have recently exhausted UI benefits. Unemployment assistance usually is available for up to a year, with the idea that it will prevent slippage into long-term dependence on social assistance by prolonging the period of hope for reemployment.15

The atmosphere of controversy surrounding specific UI issues has been intensified due to the conflict between calls for expanded welfare content in the UI program and calls for closer adherence to strict insurance principles in the face of a growing perception of general worker affluence and of a narrowed presumption of need. However, by a large margin, the public as of 1980 still regarded the payment of unemployment benefits as earned insurance rights rather than as welfare assistance. A national survey conducted in 1980 by the Survey Research Center of the University of Michigan found that almost twice as many American families characterized unemployment compensation as "earned insurance" than thought it was "part of our welfare system" (59 percent to 32 percent). "Households in which one or more members were unemployed at some time during the two years prior to the surveys more frequently viewed unemployment compensation as earned insurance, especially if the unemployed household member actually received unemployment compensation (78 percent) . . . [compared with] 56 percent of the households who had no unemployment
experience during the prior two years” (Curtin, Gordon and Ponza 1981, p. 41).

Defenders of the program’s insurance principle emphasize that UI is not intended as a measure to overcome existing poverty but rather to prevent descent into poverty. Although workers today are generally better off than their counterparts of earlier times, they still face the real risk of job loss with severe consequences. Relatively few wage or salaried workers could long withstand a total loss of their earnings before their achieved standards of living were damaged badly. Even in multiple-earner families, where the loss of one income may be partially cushioned by the remaining incomes of other household members, the loss may be severely felt because of high customary expenditure and consumer debt levels.

The lack of adequate welfare support for needy, involuntarily unemployed persons who can and want to work and who fall outside the scope of UI is a problem that the system cannot effectively resolve in its present form. Helping the poor unemployed to overcome their poverty through employment is a policy no one can oppose. Preventing workers from slippage toward poverty because of prolonged temporary job and wage loss is a more manageable task.

The values of the insurance approach go beyond that of using presumed need instead of the individual needs test. Insuring against wage loss due to involuntary unemployment makes at least as much sense as insuring a home against fire damage or a car against theft, regardless of the personal ability to absorb the financial loss. Wage loss is only partially insured, with limits applicable as to amounts and length of time. Employer payments into public funds for unemployment benefits are part of the cost of labor compensation, which includes wages and other fringe benefits. Workers earn UI rights through their employment and indirectly pay part of the premium by accepting wages that are somewhat lower than they would be in the absence of UI (Anderson and Meyer 1995). Regardless of personal financial circumstances, if their employment terminates involuntarily, workers have the right to unemployment benefits until they either find other employment or exhaust their entitlement. Unemployment benefits are not a charge on society as a whole, financed out of general government revenues, as is the case with welfare. Within the context of these UI characteristics, presumed need remains valid regardless of individual variations in need. Loss of
income can be damaging to the unemployed worker’s household finances if not limited to some reasonable degree.

Unlike private insurance payments, unemployment benefits reflect certain overtones of welfare since some of the limits satisfy social policy goals rather than purely actuarial considerations. Hence, UI is social insurance. The implicit presumption of need also has socially oriented limits. The controversy in applying limits focuses on the weekly amount and on the duration of payments.

The Role of Unemployment Insurance in the Overall Economy

One of the main reasons UI is compulsory public social insurance as opposed to private insurance is because it is the only way to achieve nearly universal coverage in the population. In performing the central income replacement function, with nearly all workers covered, the system works to arrest declining income of the unemployed, reduce the potential increase in welfare dependency, and slow the decline in aggregate spending when the economy moves into a recession. The direct cost of UI is paid by employers through payroll taxes. It has been argued that these costs affect the economy by influencing business location decisions.

In the aggregate, UI benefits constitute a nonnegligible portion of total spending in the economy. As summarized in table 1.2, between 1938 and 1995 UI benefits usually hovered in a range between one-quarter and three-quarters of 1 percent of gross domestic product (GDP). The annual figures in the table also make it clear that UI contributes a larger share of total spending in recession years than in expansion years and that the boost in spending is appreciable and rapid. For example, during the 1957-1958 recession, UI benefit payments rose from 0.39 percent to 0.77 percent of GDP, and, during the 1974-1975 recession, payments rose from 0.41 percent to 0.74 percent of GDP. Burtless (1991, p. 38) has argued that “changes in the system over the past decade have eroded the value of unemployment insurance both as income protection for the unemployed and as an automatic stabilizer.” It is easy to see in table 1.2 that the spike in benefits as a percentage of GDP was much smaller in the 1990-1991 recession than in many previous postwar recessions. This partly reflects the tighter eligibility conditions and diminished real benefit levels imposed by many of the states in response to financial crises in the early 1980s.
Table 1.2 UI Benefit Payments as Percentage of U.S. GDP, 1938-1995

<table>
<thead>
<tr>
<th>Year</th>
<th>UI benefits (thousands)</th>
<th>UI as percentage of GDP</th>
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<tbody>
<tr>
<td>1938</td>
<td>393,783</td>
<td>0.46</td>
</tr>
<tr>
<td>1939</td>
<td>429,298</td>
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<td>1940</td>
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<td>1941</td>
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<tr>
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<td>1947</td>
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<td>1960</td>
<td>2,726,849</td>
<td>0.53</td>
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<tr>
<td>1961</td>
<td>3,422,558</td>
<td>0.64</td>
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<tr>
<td>1962</td>
<td>2,675,565</td>
<td>0.47</td>
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<td>1963</td>
<td>2,775,222</td>
<td>0.46</td>
</tr>
<tr>
<td>1964</td>
<td>2,521,575</td>
<td>0.39</td>
</tr>
<tr>
<td>1965</td>
<td>2,166,011</td>
<td>0.31</td>
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<tr>
<td>1966</td>
<td>1,771,292</td>
<td>0.23</td>
</tr>
<tr>
<td>1967</td>
<td>2,092,364</td>
<td>0.26</td>
</tr>
<tr>
<td>Year</td>
<td>UI benefits (thousands)</td>
<td>UI as percentage of GDP</td>
</tr>
<tr>
<td>------</td>
<td>-------------------------</td>
<td>-------------------------</td>
</tr>
<tr>
<td>1968</td>
<td>2,029,957</td>
<td>0.23</td>
</tr>
<tr>
<td>1969</td>
<td>2,125,809</td>
<td>0.22</td>
</tr>
<tr>
<td>1970</td>
<td>3,847,312</td>
<td>0.38</td>
</tr>
<tr>
<td>1971</td>
<td>5,935,925</td>
<td>0.45</td>
</tr>
<tr>
<td>1972</td>
<td>4,520,809</td>
<td>0.37</td>
</tr>
<tr>
<td>1973</td>
<td>4,090,573</td>
<td>0.30</td>
</tr>
<tr>
<td>1974</td>
<td>6,107,448</td>
<td>0.41</td>
</tr>
<tr>
<td>1975</td>
<td>11,986,137</td>
<td>0.74</td>
</tr>
<tr>
<td>1976</td>
<td>9,305,600</td>
<td>0.51</td>
</tr>
<tr>
<td>1977</td>
<td>8,666,091</td>
<td>0.42</td>
</tr>
<tr>
<td>1978</td>
<td>7,998,880</td>
<td>0.35</td>
</tr>
<tr>
<td>1979</td>
<td>9,241,720</td>
<td>0.36</td>
</tr>
<tr>
<td>1980</td>
<td>14,191,178</td>
<td>0.51</td>
</tr>
<tr>
<td>1981</td>
<td>13,879,278</td>
<td>0.44</td>
</tr>
<tr>
<td>1982</td>
<td>21,100,164</td>
<td>0.65</td>
</tr>
<tr>
<td>1983</td>
<td>18,510,200</td>
<td>0.52</td>
</tr>
<tr>
<td>1984</td>
<td>13,231,491</td>
<td>0.33</td>
</tr>
<tr>
<td>1985</td>
<td>14,682,332</td>
<td>0.35</td>
</tr>
<tr>
<td>1986</td>
<td>15,950,231</td>
<td>0.36</td>
</tr>
<tr>
<td>1987</td>
<td>14,190,743</td>
<td>0.30</td>
</tr>
<tr>
<td>1988</td>
<td>13,240,757</td>
<td>0.26</td>
</tr>
<tr>
<td>1989</td>
<td>14,205,321</td>
<td>0.26</td>
</tr>
<tr>
<td>1990</td>
<td>17,975,980</td>
<td>0.31</td>
</tr>
<tr>
<td>1991</td>
<td>25,478,724</td>
<td>0.43</td>
</tr>
<tr>
<td>1992</td>
<td>25,066,162</td>
<td>0.40</td>
</tr>
<tr>
<td>1993</td>
<td>21,758,380</td>
<td>0.34</td>
</tr>
<tr>
<td>1994</td>
<td>20,979,858</td>
<td>0.30</td>
</tr>
<tr>
<td>1995</td>
<td>21,278,429</td>
<td>0.29</td>
</tr>
</tbody>
</table>

When we look at the dollars of UI benefits as a share of GDP, we see only the direct first-order effect of UI on aggregate spending. It should be recognized that spending of UI benefits becomes money income to others who again spend a part of it, and so on. The cumulative effect of all the spending is called the multiplier. For the nation as a whole, Oaxaca and Taylor (1983, p. 6) estimated that “for each dollar of UI benefit payments in 1975 . . . disposable income was increased by $1.02.” Percentage effects estimated by Oaxaca and Taylor (1986) of UI benefit payments on local economies were even larger, at 3.18 percent of real disposable income in Phoenix and 2.16 percent in Tucson for 1976.17

UI is also considered to have an impact on the economy because of the payroll tax charged to employers to finance the system. While Anderson and Meyer (1995) estimate that this cost is partly shared by workers who contribute to the system by accepting lower wages, it has been argued widely that UI taxes are one of the factors figuring into business decisions about where to locate or to expand operations. This thesis was put forward more generally in terms of all area-specific tax levies by Due:

On the basis of all available studies, it is obvious that relatively high business tax levels do not have the disastrous effects claimed for them. . . . However, without doubt, in some instances the tax element plays the deciding role in determining the optimum location, since other factors balance (Due 1961, p. 171).

Interstate variation in business taxes was examined by Wheaton (1983), who suggested that these differences may affect business location decisions within small geographic areas such as at interstate borders. Among individual categories of taxes that vary across states, Wheaton (1983, p. 85) estimated that property taxes constitute 42 percent of tax payments; UI taxes are tied for second with state corporate income taxes, each of which receives 18 percent of total state tax payments made by business. In a survey article, Newman and Sullivan (1988, p. 232) conclude that “the most recent studies, employing more detailed data sets and more refined econometric techniques, have generated results which cast some doubt on the received conclusion that tax effects are generally negligible.” While the role of UI as a built-in economic stabilizer is widely acknowledged as significant and useful, interstate differences in the employer cost of the program remain an area of constant controversy.
Unemployment Insurance as Part of the Social Safety Net

The social safety net in the United States is an intertwined web of public and private programs that naturally divide into two main categories. One group of programs is for labor force members with a reasonable history of job attachment; eligibility for these programs is usually independent of individual or household income levels. The other group provides benefits without regard to attachment to the labor force and generally requires a low-income test. UI may be viewed as a keystone in the arch supporting that portion of the U.S. social safety net designed for workers attached to the labor force.

In testimony before the Subcommittee on Department Operations, Nutrition and Foreign Agriculture, Committee on Agriculture of the U.S. House of Representatives, Jane L. Ross, Director for Income Security Issues of the U.S. General Accounting Office, provided an overview of means-tested programs:

In fiscal year 1992, the federal government provided about $208 billion in six areas of need for low-income people. When state dollars are included, the total amount of spending reached $290 billion.

The welfare system comprises about 80 programs, representing about 15 percent of total federal outlays in fiscal year 1992. Included in the system are AFDC, Medicaid, SSI, and Food Stamp programs. These four means-tested programs accounted for 20 percent of the $700 billion spent in fiscal year 1993 on the 10 largest entitlement and mandatory spending programs.[18] The system's nearly 80 programs target low-income individuals and families to meet two broad objectives: (1) to provide basic support and health care for those who are often unable to support themselves—the aged, blind, disabled, and children—and (2) to provide transitional assistance to able-bodied adults and their families while promoting self-sufficiency. table 1 [1.3] highlights the federal spending levels in some of the largest programs in each area (Ross 1995, p. 2).
Table 1.3 Selected Means-Tested Programs in Six Functional Areas (Dollars in Billions)

<table>
<thead>
<tr>
<th>Functional area/program</th>
<th>FY 1992 estimated expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income support</strong></td>
<td></td>
</tr>
<tr>
<td>Aid to Families with Dependent Children</td>
<td>$13.6</td>
</tr>
<tr>
<td>Supplemental Security Income</td>
<td>18.7</td>
</tr>
<tr>
<td>Earned Income Tax Credit (EITC)</td>
<td>9.6</td>
</tr>
<tr>
<td><strong>Medical care</strong></td>
<td></td>
</tr>
<tr>
<td>Medicaid</td>
<td>67.8</td>
</tr>
<tr>
<td>Medical Care for Certain Veterans</td>
<td>7.8</td>
</tr>
<tr>
<td><strong>Food and nutrition</strong></td>
<td></td>
</tr>
<tr>
<td>Food Stamps</td>
<td>23.5</td>
</tr>
<tr>
<td>School Lunch</td>
<td>3.9</td>
</tr>
<tr>
<td>Special Supplemental Food Program for Women, Infants and Children (WIC)</td>
<td>2.6</td>
</tr>
<tr>
<td>School Breakfast</td>
<td>.8</td>
</tr>
<tr>
<td><strong>Housing</strong></td>
<td></td>
</tr>
<tr>
<td>Section 8 Housing Assistance</td>
<td>12.3</td>
</tr>
<tr>
<td>Low-Rent Public Housing</td>
<td>5.0</td>
</tr>
<tr>
<td><strong>Education and training</strong></td>
<td></td>
</tr>
<tr>
<td>Stafford Loans and Pell Grants</td>
<td>11.1</td>
</tr>
<tr>
<td>Job Training Partnership Act (JTPA)</td>
<td>3.9</td>
</tr>
<tr>
<td>Head Start</td>
<td>2.2</td>
</tr>
<tr>
<td>Job Opportunities and Basic Skills (JOBS) Training Program</td>
<td>.6</td>
</tr>
<tr>
<td><strong>Other services</strong></td>
<td></td>
</tr>
<tr>
<td>Social Services Block Grant (SSBG)</td>
<td>2.8</td>
</tr>
<tr>
<td>Child Care and Development Block Grant (CCDBG)</td>
<td>.8</td>
</tr>
<tr>
<td>Child Care—AFDC, Transitional, and At-Risk</td>
<td>.8</td>
</tr>
<tr>
<td>Community Services Block Grant (CSBG)</td>
<td>.4</td>
</tr>
</tbody>
</table>

SOURCE Ross (1995, p. 3).
Many industrialized nations bridge the gap between UI and welfare with a program of *unemployment assistance*, which is a means-tested benefit for people who have recently exhausted UI benefits. In the United States, while the duration of UI benefit payments may be extended depending on the condition of the economy, there is no standard benefit program to help individual UI benefit exhaustees in the absence of a widespread recession.

Apart from UI, the main body of public programs for people with labor market attachment or aspirations consists of retraining programs. In testimony before the U.S. Senate Committee on Labor and Human Resources, Clarence C. Crawford, Associate Director of the U.S. General Accounting Office for Education and Employment Issues, stated that

. . . legislation enacted in the last Congress identified at least 163 programs administered by 15 different agencies that provide about $20 billion in employment training assistance for adults and out-of-school youths...“employment training programs” refers to programs or funding streams that (1) help the unemployed find jobs, (2) create job opportunities, and (3) enhance the skills of participants to increase their employability (Crawford 1995, p. 1).

This list includes everything from the Food Stamp Employment and Training program administered by the U.S. Department of Agriculture to improve the ability of food stamp recipients to gain employment, increase earnings, and reduce their dependency on public assistance, to the All-Volunteer Force Educational Assistance program administered by the U.S. Department of Veterans Affairs, which aims to assist in developing a more highly educated and productive workforce by helping service-persons readjust to civilian life through educational benefits. The complexity of eligibility conditions and benefits available from the 163 different federal employment and training programs has spurred efforts to establish a unified “one-stop-shopping” training system.

The reemployment system most closely linked to the UI system is the state-operated Employment Service (ES). While there have been calls for a new institution to act as a reemployment clearing house, the ES has been touted by some as the natural point of entry for one-stop shopping. The ES is an existing agency with a statutory funding stream
authorized by the Wagner-Peyser Act, and it has strong state relationships with existing offices in 1,700 locations.

The widespread ES presence has also raised the issue of whether a newly proposed one-stop reemployment services delivery system needs another physical institution. Simultaneously, there is recognition of the prospect that the new institution could be a virtual one-stop-shopping place for reemployment services, operating in cyberspace as an electronic network among existing physical locations. Eligibility for various programs and options available to an individual could be determined through the electronic information network. Under virtual one-stop shopping, the system would be most encompassing if any existing agency could serve as a port of entry, so that there would be one-stop shopping with multiple points of entry.

The ES link with the UI system was forged through cooperation in enforcing the work test for UI benefit eligibility. Further links have been provided since 1982, as the ES has been involved in referring beneficiaries who exhaust UI entitlement to retraining programs administered under the Job Training Partnership Act (JTPA). The most recent reemployment initiative in UI, the Worker Profiling and Reemployment Services (WPRS) system, has relied heavily on the ES to provide early intervention reemployment services to UI claimants identified as being most likely to exhaust benefits.

Historically, there has been a general reluctance to fund active labor market programs other than the ES from the Unemployment Trust Fund. Congress and the executive branch have faced strong opposition from the employer community regarding possible funding of retraining and other reemployment services from the Unemployment Trust Fund. Employers believe that active labor market programs should be paid for out of general revenue and question their responsibility for training the potential workforce of competitors. Since the Unemployment Trust Fund frequently contains a large reserve for recessionary periods, it has often become the target for alternative uses when reserves increase during periods of low unemployment.19

With increased concern about maintaining employment and returning unemployed workers to productive jobs, the UI program has taken a more active role in reemployment policy. UI funds are being used to pay for two types of active employment efforts: work sharing, which is a form of partial UI benefits, and self-employment allowances, which
are UI benefits received while starting a new business. On the other hand, there is no movement to allow the Unemployment Trust Fund to pay for retraining or reemployment services such as job search assistance. Under the WPRS initiative, the UI program conducts profiling, but the provision of reemployment services, such as testing, counseling, job clubs, and job search workshops, cannot be funded by the UI system. These services must be provided by the ES or the JTPA program. Together, these active labor market efforts are linking UI with initiatives that strengthen the social safety net and help labor force members from slipping toward public support.

**Incentives for Job Search and Employment**

Along with the view that the unemployed generally could find work if they wanted to is a related belief that the payment of unemployment benefits diminishes the recipient's incentive to work or to seek work. The disincentive argument has been made against UI since the earliest days of its consideration. It is part of the philosophy that social programs weaken the work ethic, sap self-discipline, and create a growing dependence on transfer payments that “have imposed a rising burden of taxation on working families which has provoked a spirit of anger and frustration with American democratic institutions” (Gilder 1981, p. 137). This threat of moral decline and malingering has been the prime argument by opponents to broadening the UI system.

During the 1970s, when many states constrained weekly benefit amounts and the duration of benefits they provided, even as unemployment levels were rising, the disincentive case was pressed more forcefully. Higher unemployment rates were alleged to be due, at least in part, to generous UI benefits. These charges relied on a body of research that empirically tested for evidence of the effects of unemployment benefits on the level and duration of joblessness. Researchers attempted to measure how changes in various parameters of the program, like the weekly benefit amount, the wage replacement rate, and the entitled duration of benefits, influenced the duration of insured unemployment. No two studies were exactly comparable. They differed with respect to the types of data used, the specifications of the
hypotheses to be tested, the definitions of the variables, the behavioral assumptions adopted, and the kinds of analytical approaches applied.\textsuperscript{20}

Despite their noncomparabilities and varying results, the studies did supply evidence in support of the effects hypothesized. For example, after reviewing the methodology and findings of a dozen studies of the effects of UI on the duration of unemployment, Hamermesh concluded that

\[
\text{the best estimate—if one chooses a simple figure—is that a 10-}
\text{percentage point increase in the gross replacement rate leads to an}
\text{increase in the duration of insured unemployment of about half a}
\text{week when labor markets are tight. This is not an exact figure, but}
\text{it does appear that there is some effect, certainly above zero and}
\text{probably less than one week (Hamermesh 1977, p. 37).}
\]

The findings of these studies suggest that increased UI liberality reduces the incentive to return to work. Research about the size and significance of the work disincentive has continued. Some analysts have advanced the countervailing thesis that, by allowing recipients to search more extensively for suitable work, improved benefits enhance the efficiency of the labor market. Thus, a rise in unemployment duration could prove beneficial to the economy as well as to the recipient in the longer run. Attempts to measure the favorable job search effects of UI have been few and have not been regarded as satisfactory (Welch 1977). Overall, findings from research done in this period provided some support for stricter benefit eligibility rules and less generous payment levels so as to minimize work disincentives.

It was argued that the narrow gap between the net after-tax wage workers might earn on a job and the weekly UI benefit amount was an important element contributing to the disincentive effect of unemployment benefits. Feldstein (1974) focused on this factor and showed how taxes withheld from wages could severely limit the monetary advantage of working over drawing benefits. His analyses helped to support the case for taxing unemployment benefits as income, a policy adopted beginning in 1979 for recipients in households with incomes above specified levels, and applied universally regardless of income levels beginning in 1986. A study by Solon (1985), examining the experience in Georgia during the first year the new tax policy took effect, provided some evidence that benefit recipients at income levels subject to the tax
had a significantly shorter duration of unemployment, on average, than recipients at similar income levels the year before the tax applied. Recipients at lower income levels showed no reduction in average duration levels over these two years.

The work disincentive argument, fortified by the research findings, was used by those who wished to curtail the liberality of the UI program. The taxation of benefits was a direct outcome of this movement. As Vroman (1990) documents, the benefit funding crises experienced by many states following the back-to-back recessions of 1980 and 1982 exerted further pressure on the states to restrict benefits and to tighten eligibility rules.

More recent studies of UI work disincentive effects have used different or refined research methodologies. Katz and Meyer (1990) produced some of the biggest disincentive effect estimates yet. They found that a 10 percentage point rise in the UI wage replacement rate increased the average duration of insured unemployment by 1.5 weeks. Davidson and Woodbury (1996) have found estimates closer to results from studies done in the 1970s. Using an equilibrium search and matching model calibrated with data from several UI field experiments conducted in the 1980s, they found that a “10 percentage point increase in the UI wage replacement rate can be expected to increase the unemployment duration of UI claimants by between 0.3 and 1.1 weeks” (Davidson and Woodbury 1996, p. 25).

Among both researchers and policy makers, there has recently been great interest in positive reemployment incentives for UI beneficiaries. While stricter eligibility rules with respect to job search requirements may be considered something of a stick, the spur to reemployment efforts is viewed more as a carrot. Positive reemployment incentives have appeared as a natural alternative to further costly administrative monitoring of compliance with work search requirements. The Office of the Chief Economist of the U.S. Department of Labor summarized research findings from a variety of experiments testing new reemployment incentives for UI beneficiaries. Field experiments involving randomized trials of various positive reemployment incentives for UI beneficiaries have been conducted in the states of Illinois, Massachusetts, New Jersey, Pennsylvania, and Washington. These incentives have included cash bonuses, self-employment allowances, referral to retraining, and individually tailored job search assistance. The experi-
ments have led the way to federal legislation permitting states to offer self-employment allowances and requiring referral to job search assistance for some UI recipients.

The compulsory initiative to come out of the research on positive reemployment incentives for UI claimants, the Worker Profiling and Re-employment Services system, was required by legislation enacted in 1993. This system has given a new, positive role to the cooperative agreement between UI and reemployment service providers—the public employment service and the JTPA system. Previously, the only link between the two organizations was that, in most states, the employment service helped to enforce the UI work test, largely through registration with the employment services as well as with some placement efforts. For claimants identified as being most likely to exhaust UI benefits, participation in reemployment activities is an additional eligibility requirement for continued benefit receipt.

**Fraud and Abuse**

To qualify for UI benefits, in addition to being involuntarily separated from work, the individual must want employment, be able to work, be available and prepared to take a suitable job, and make appropriate efforts to regain employment. These conditions are imposed in an attempt to affirm that unemployment is an insurable risk, that is, to reduce the *moral hazard* in UI, the risk of compensating malingering rather than genuine unemployment. An individual’s unemployment following a job separation can be, to a greater or lesser degree, a function of how much he or she truly wants to work. The worker files for UI benefits for each week claimed as a week of unemployment. It is administratively very difficult to monitor whether the worker is earnest about actually becoming reemployed. This is a classic example of the *principal-agent* problem, which is familiar in private insurance markets. Unless the claimant admits a lack of interest in working, there is no objective way of assessing the genuine desire for work, short of being able to offer a suitable job opportunity. The UI system seeks evidence in other ways, mainly on the basis of the individual’s pattern of behavior or circumstances, which might indicate a weak interest in
working. This largely subjective approach is a difficult one to administer. It is a process open to a wide range of judgment; it is fraught with suspicion and uncertainty and is frequently contentious.

Historically, certain kinds of UI claimants have tended to arouse more suspicion about their reemployment intentions than others. These include spouses of fully employed workers, students and other teenagers living with their parents, workers between seasonal jobs, and pensioners. Since involuntary unemployment is difficult to prove in so many situations, one school of thought holds that the provisions of UI law should be strict enough to ensure that benefits go to only those who are unquestionably and demonstrably involuntarily unemployed. The other school of thought holds that the unemployed worker should be given the benefit of the doubt and that the law should be liberal in testing the readiness of the worker to find employment. This philosophical difference partly explains the variation in eligibility rules across states. It also helps to explain the variation in the severity of the disqualifications imposed. For example, the first school of thought would apply blanket disqualifications to all persons who quit their jobs to relocate geographically with a moving spouse. Those holding to the second school of thought would permit the payment of benefits to such workers if they demonstrated that they were available and able to work in the area of their new residence. In fact, there has been a gradual tightening of eligibility conditions for a wide variety of causes, and there has been a similar tightening of disqualifications from receiving benefits from a fixed time period to the entire duration of the spell. This has been a fight that benefit rights advocates have gradually but steadily lost in the states.

The subjective character of unemployment is an important factor contributing to the differential treatment of claimants across jurisdictions. Apart from variations in statutory provisions that reflect opposing schools of thought, there are differences among the states in administrative policies and procedures as they are applied in determining the validity of claims. The potential for abuse in this troublesome area, both by the claimant and of the rights of the claimant, constitutes another source of controversy for the program.

The perception of the extent to which beneficiaries abuse the UI program affects attitudes toward many of its provisions. Periodically, the system has been subject to attacks in the news media, which attempt to
prove, or at least to imply strongly, that benefits are being paid to large numbers of "loafers, quitters, schemers and cheaters." The instances of abuse described run the gamut of situations involving violations of specific provisions in many of the state laws. Examples cited often include students, pregnant women, women who have quit their jobs to fulfill marital obligations, seasonal workers, and vacationers, all of whom, in the opinion of the critic, are not very interested in taking work and therefore abuse the system by drawing benefits. Disqualification provisions for voluntary quitting or discharge for misconduct are attacked as being too lenient and leading to abuse of the system. The cases are not always situations in which outright fraud is perpetrated but include ones in which the worker is alleged to have taken advantage of some provision or interpretation of the law in a manner that constitutes an abuse. The criticism is directed at the offending provision as one allowing the payment of benefits when it should not. These cases generally are not run-of-the-mill examples but are unusual ones that, in most instances, have been the subject of review by appeals tribunals, even by the courts, and in which benefits have been awarded. Such cases are usually on the borderline; otherwise, they would not have reached the appeal stage. The U.S. Department of Labor has often found that the facts cited by the critics are taken out of context and fail to include the extenuating circumstances that led to the final award of benefits (U.S. Department of Labor 1960). Occasionally, a presumably fraudulent case is identified in the media with information not previously available to the administrative agency. Given this information, the agency would not pay the benefits. The media criticisms often select particular cases because they support an attack on the legal provisions that permit the payment of benefits in such instances.

Given the criticisms of the mid-1970s and the mounting pressures exerted by the financial strains most state programs experienced, it is not surprising that the trend turned strongly in the direction of stiffer eligibility rules, more severe disqualifications, and tighter administration. The first move was a broadened and strengthened application of work search rules. Many states increased requirements for claimants to furnish specific evidence of their job search, usually by indicating the names of a minimum number of employers contacted each week.

In response to concern about the potential for fraud and abuse in the UI system, Burgess and Kingston (1980) undertook a six-city study of
the accuracy of benefit payments for the National Commission on Unemployment Compensation. They estimated that 50 percent of benefit overpayments identified by intensive study, ex post, were due to either the “failure of claimants to conduct active job searches or by claimants’ unavailability for work” (Burgess and Kingston 1980, p. 508). These findings led to more comprehensive research to develop and test a method to intensively audit a random sample of claims paid. Such a study was conducted in five states between April 1981 and March 1982. The results from this more involved investigation indicated that about 14 percent of all benefits paid in these states during the period were in excess of the entitled amount. Furthermore, the principal reason for the overpayments, accounting for nearly half to four-fifths of the total amounts overpaid in each of the states, was inadequate work search—failure to meet the work search requirement which was not detected when the claim was filed and processed for payment.

Beginning in calendar year 1988 as the Benefits Quality Control Program, the random sample audit procedure was introduced as a standard operation throughout the nation. It has produced estimates of error rates similar to those found in the pilot studies. In calendar year 1993, for all states reporting, the estimated error rate was 8.8 percent of a total of $21.05 billion in benefit payments. This error rate is in line with rates of the last few years, but lower than estimated in the first few years that benefit payment accuracy was checked by random audit.

The trend among the states toward stiffer enforcement of the work test was reversed following nationwide implementation of the Benefits Quality Control Program. It may be the case that the relaxed stringency of the work test is due to an effort on the part of the states to lower their error rates, and to perform better on the quality control random audit, since failure of the work test remains a prime reason for payment errors.

 Debate continues over whether an active weekly work search requirement applied generally to claimants contributes much to speedier reemployment in many cases. Reasonable and useful job search may call for different approaches, depending on a claimant’s occupation and experience, on the recruiting and hiring practices of potential employers, and on the current condition of the labor market. Many states provide for certain exemptions or departures from their active search requirements to reflect these practical realities. This approach
makes for even more complexity but attempts, at least, to minimize fruitless efforts by claimants and annoyances to employers that serve only to satisfy a bureaucratic rule but do not lead to reemployment. Is the evidence of substantial overpayments of benefits an indication of widespread abuse? Of a lack of interest in work? Would stricter enforcement of the work search requirements eliminate many benefit payments, or would it induce claimants to make more effort to meet the requirements even if it served no other purpose?

Up until recently, the work test was generally a mechanical process: if individuals indicated that they were able and available for work, and if they listed three separate employer job search contacts or, in some states, simply indicated that they searched for work, usually nothing else was done by the state agency. Some states claim to check the validity of listed work searches contacts; this is unlikely.

The decline in the UI work test is mostly in the elimination of the certification of having searched for work with a given number of employers in the previous week and naming those employers on the continued claims form. These changes may partially reflect an effort to reduce reported error rates under the Benefits Quality Control Program.

A field experiment conducted in Tacoma, Washington, investigated whether the traditional work test of requiring three employer contacts reduced UI benefit duration and payments relative to no work test or to significantly more intensive work search requirements. Based on this experiment, Johnson and Klepinger (1994) estimated that, if UI checks continue with self-certification for continued receipt and no reporting requirement, benefit duration will increase by 3.3 weeks relative to the traditional work test. In addition, they found that significantly more aggressive work search assistance is likely to shorten benefit duration by about half a week as compared to the customary three contacts work test. The evidence from Washington resulted in the U.S. Department of Labor funding an additional alternative work search experiment in Maryland.28

There is no doubt that there are cases in which claimants take advantage of provisions in state laws that permit some latitude in interpretation. Recent trends have lowered that latitude and, thus, have reduced opportunities for abuse. The tightening of eligibility rules and stiffened enforcement have also eliminated some claims that were previously
regarded as valid and free of any questions. To the extent that the public sees UI abuse as a serious problem, the program will be controversial in those areas suspected of vulnerability to such practices.

In evaluating the overpayments issue, Kingston, Burgess, and St. Louis (1983), who pioneered the random audit procedure, noted certain "features of the unemployment insurance program which contributed significantly to the problem." Prominent among these were the complexity of the program's eligibility provisions and policies, the limitations in administrative resources that made it unlikely that agency staff could monitor claimant compliance with the rules effectively and equitably, and the weaknesses in the program's incentives for detecting and restraining improper payments.29 Reflecting more broadly on ways to reduce problems of fraud and abuse, Burgess and Kingston identified six desirable features of a UI system:

(1) appropriate economic incentives for all system participants, including strong incentives for claimant self-compliance; (2) to the extent possible, simple rather than complex system features and eligibility criteria; (3) to the extent possible, little emphasis on intensive administrative scrutiny of claimant behavior and motives in the routine operational system, with emphasis instead placed on self-compliance with relatively objective and easily measurable criteria; (4) minimizing the administrative discretion that makes selective application and enforcement of eligibility criteria possible; (5) horizontal equity for system participants; and (6) incentives for both administrative efficiency and smaller administrative bureaucracies (Burgess and Kingston 1987, pp. 258-259).

Conflicting Employer and Labor Views of the System

Long before the establishment of the federal-state UI system in the United States, both employers and labor opposed it as a compulsory public program, although for different reasons. Labor's reservations were founded in suspicions developed following many years of consistent hostility by government authorities toward worker efforts to organize and to press demands for better wages and working conditions. The principal union leadership stood against any governmental
involvement in labor-management relations and preferred to deal directly with management to resolve mutual problems. It was not until 1932 that the position of organized labor shifted to support for UI.

Employer opposition was also rooted in history as well as in classical economic theory. Starting with the decline of feudalism and continuing through the industrial revolution to the dominance of modern corporate enterprise, the tradition of employer responsibility for the personal welfare of employees weakened to the vanishing point. Individual employers could and did sympathize with individual workers who suffered the hardships of unemployment, but this was usually separated from any economic responsibility. Applying classical economic theory, unemployment was viewed as the result of a temporary imperfection, an imbalance in the market that was readily corrected as wages adjusted to levels at which the demand for labor would absorb the excess supply. Tampering with the operation of this mechanism, such as by government intervention, was thought to endanger the corrective process and to possibly delay or prevent the restoration of equilibrium at full employment. In this context, UI was regarded as interference in the market adjustment.

The massive and prolonged unemployment of the depression damaged the credibility of classical economic theory. The theory held that, in the long run, prices would adjust so that markets would clear, meaning that unemployment would vanish. In response to this line of thinking, John Maynard Keynes, who advocated government management of aggregate spending in the economy and who changed the way economists view severe economic recessions, wrote that "in the long run we're all dead" (Heilbroner 1953, p. 251).

Although the momentum for UI began to build, employers generally held to their opposition. Since the proposed plans placed most or all of the UI financial burden on employers, their opposition focused on the taxes to be levied on them. The UI taxes were viewed as a further impediment to business, at a time when most were struggling to stay afloat, and as a competitive disadvantage in interstate commerce (Ewing 1933, p. 13). Moreover, the tax reversed historic trends by compelling employers to assume some responsibility for the welfare of their employees, representing another step back from free enterprise. Opposition on these grounds was expressed by Noel Sargent of the National Association of Manufacturers before a select committee of
the United States Senate in 1931: "Penalization of employers because of unemployment resulting from conditions over which the employer has little control is both ethically and economically unjustified" (U.S. Senate 1931).

The injection of experience rating into the UI system made the program more acceptable to employers. It was reasoned that, by allocating benefit costs to those businesses giving rise to compensated unemployment, experience rating helped to keep UI consistent with the free market system. The costs of the goods and services produced by insured workers thus would also reflect the costs of benefits paid to them if they experienced involuntary unemployment. Because of market competition, employers, seeking to minimize costs, are motivated to avoid or minimize unemployment of their workers. In this way, it is argued, experience rating serves the twin goals of appropriate economic cost allocation and employment stability. Furthermore, the tax offset scheme introduced by the Federal Unemployment Tax Act of 1935 allayed most fears about competitive disadvantage across states.

These theoretical concerns were prevalent before 1935, when the Social Security Act required states to establish UI systems. After the system was up and running, there was an added practical concern by employers about experience rating. As noted earlier, UI costs at the outset were on the whole less than they were expected to be and well under the standard tax rates levied by the states. The only way allowed under the system to reduce tax rates was through experience rating. As experience rating spread and tax rates declined, many employers became increasingly sensitive to benefit costs and to charges against their accounts.

The concept took hold among employers that they should pay only the cost of benefits related to their own layoffs of workers. This view is a major reason for general employer advocacy of many restrictions on benefit payments to workers whose unemployment is not attributable to their employers. Labor has opposed experience rating, claiming that it leads employers to be restrictive about their employees’ benefit rights and to challenge claims unjustifiably so as to keep down charges and tax rates.

Labor and management have been natural antagonists with respect to UI. Employers generally resist any expansion or liberalization that would add to costs. Labor’s interest is to press for generous levels of
benefit support during unemployment, for as long a period as necessary, with relatively few restrictions on eligibility. The confrontation of these diametrically opposed interests assures conflict on nearly every aspect of the program.

Since specific UI elements are defined by law, the conflict usually centers on the legislative process, mostly at the state level. The detailed provisions of state law are of prime importance to employers, individually and collectively, given their sensitivity to cost. Few sophisticated employers feel that they can stress or even discuss candidly their concern over costs. Much of their discussion and debate deals with less tangible matters such as "insurance principles," "equities," "abuses," and "work disincentives," arguments that play useful roles in legislative maneuvering. On the other side, labor's efforts stress the hardships endured by the unemployed and the inadequacy of UI benefits to alleviate deprivation and suffering. Not all employer and labor representatives hold unreservedly to these positions. Many come to a responsible conclusion with a balanced resolution of the conflict. At times, the two sides may bring an agreed upon bill before the state legislature, the result of concessions and compromises. This approach does not always serve the public's best interest, however, if employers agree to a benefit increase in return for labor's agreement not to oppose a tax reduction, with the solvency of the fund weakened in the process.

Throughout much of the program's history, employer influence at the state level in many parts of the country has been greater than that of labor in shaping UI provisions. Where union strength has been more concentrated, as in heavily industrialized states, the results have been more balanced. Labor, however, has felt that its views have received a better response at the federal level than in the states, at least until 1980. Labor has favored more federal UI control, such as through the imposition of minimum benefit standards, and even complete federalization of the program, arguing that unemployed workers have been treated inadequately and inequitably under widely disparate state laws. Employers oppose increased federal control of the program, usually on the basis of political philosophy, arguing the dangers and inefficiencies of operation or dominance by a remote, cumbersome central government.

Beginning in the late 1970s and continuing into the 1990s, the federal government has increased the number of federal compliance rules
that affect the discretionary authority of states over their own UI laws. However, these changes have not usually been supportive of organized labor's goals for the program. Union membership in the United States has declined dramatically in the past half century, falling from 35.5 percent of the work force in 1945 to 15.8 percent in 1995 (*1995 World Almanac and Book of Facts*, p. 154). The influence of organized labor has in advocating its UI objectives has accordingly diminished. The financial difficulties encountered by many of the states in the 1970s, 1980s, and 1990s have pushed UI taxes higher despite the usual employer resistance. It seems fair to say, however, that some of the past extremes of the employer-labor UI controversy have eased somewhat. Responsible leadership on both sides is usually able to reach some reasonable accommodation to protect the system's basic integrity. Moreover, the narrower employer and labor concerns are giving way more often to broader public considerations.

**Federal-State Relationships and Conflicts**

The decision at the outset to establish UI as a federal-state system did not end striving for a wholly federal system after the program began. Champions of the federal approach, some of whom held important staff positions at the Social Security Board, pressed their case strongly during World War II, when the state employment services were nationalized. As noted earlier, the Board itself recommended that UI also be converted to a uniform federal program. The Truman administration opposed the return of the employment service to the states after a period of wartime federalization. State officials successfully organized themselves to help defeat attempts to eliminate or to reduce their role in the employment service at that time. As a result of these early experiences and later because of a states' rights philosophy, state employment security administrators generally looked upon nearly all subsequent federal legislative proposals to broaden UI as efforts to assert greater federal control over the system, even well after any active hope for federalization had been abandoned. Opposition to these proposals frequently was ideological and did not address their intrinsic merits.
Throughout much of the first four decades of the UI program, employer groups allied themselves with state administrators in opposing liberal federal proposals, which labor tended to support. Not all state officials lined up in the same way during this period, but the majority of them did. On the whole, this combined opposition succeeded in blocking, slowing, or limiting changes in the system through federal laws. For example, federal minimum benefit standards have been proposed repeatedly, often with broad support, as a means of overcoming the persistent failure of the majority of states to provide adequate benefit levels under their own provisions. On a few occasions, one or more of the proposed standards came close to passage, but in the end, none was ever adopted. Preference for retention of state control of these matters was a major factor in the outcome, even in cases of acknowledged program inadequacies.

The federal role in the UI system, nevertheless, did expand as the result of two major developments beginning in the 1970s. One was the permanent provision of extended benefits for the long-term unemployed during periods of high unemployment, as mandated by the permanent federal-state shared program adopted by Congress in 1970. The other development was the widespread insolvency of state UI funds during the 1970s and 1980s, which called into play the provisions of the federal loan fund. Repeated use of federal-state shared extended benefits plus wholly federal supplemental extensions during the 1970s and 1980s gradually increased the number of federal rules applicable to benefit entitlement provisions, which heretofore had been exclusively state concerns. Although the federal rules applied only to the extended and supplemental benefits, they could not help but influence regular state benefits as well.

The financial problems of the period produced even more pervasive federal influence over state programs. Blaustein (1993, chapter 9) describes how the evolution of federal loan and repayment provisions structured incentives and penalties that have induced states in debt to restrict benefit eligibility and benefit levels and to increase tax levies in order to overcome insolvency. During the 1980s, a number of federal requirements were also enacted that had some direct impact on state benefit provisions; in effect, these amounted to federal benefit standards. In these cases, however, the requirements operated to make states pay less rather than more in benefits. It is ironic that such federal
provisions circumscribing state control should have been put through by a Reagan administration that was publicly committed to reducing the power and role of the federal government and to strengthening the role of the states in the interest of a “new federalism.” The basic purpose of these provisions, however, was to lower the costs of the UI program, and this could be done expeditiously only by amending federal law with respect to the federal, rather than state, UI programs.

There has been an uneasy balance of power between the states and the federal government over the administration of the UI program. Federal law specifies broad administrative standards to which the states must conform. States are free to structure and operate their UI programs within these broad constraints. Over time, federal constraints have declined. Highly detailed budgeting in the 1950s and 1960s—when the purchase of individual capital equipment items had to be approved by the U.S. Department of Labor—changed to broader categorical grants in the 1970s. Finally, the states were given “bottom line” authority between grant categories beginning in 1986. Despite this gradual relaxation of administrative rules, over the years, this entire area has been a source of friction between the two partners in the system. In the mid-1980s, the Reagan administration moved to alter that arrangement by proposing “devolution.” The federal government would surrender many of its responsibilities for and power over state program administration. It would also reduce the federal unemployment tax by an amount equivalent to that portion going to support state program administration. States would then be left free to determine how they preferred to administer their own programs and how to finance the costs involved. Despite years of federal-state controversy, as of 1997, the system for financing state administration remains unchanged. Many states have claimed that a fair share of administrative financing dollars has not been returned to them because of federal efforts to reduce the persistent annual federal budget deficits. Meanwhile, in the face of rapid improvements in information processing capabilities, there has been no agreement on what constitutes efficient administration of UI.

The nature of the federal-state system is such that some conflict between the two partners is inevitable. Given the federal structure of our governmental arrangements, it would appear that the particular UI approach chosen offered a means of serving urgent national economic
needs while preserving the state and local fabric that comprises the web of our society. The balance is a delicate one, never perfect, and often in flux. Some critics of the federal-state approach to UI see the problem of unemployment as increasingly countrywide, requiring a national remedy. Others see the problem as varied as the nation’s geography and believe the solution cannot lie in application of broad uniform standards; they favor more state control and experimentation, out of which would emerge better solutions. Still others feel that the existing system provides the framework for debate yielding the best balance of federal and state ideas.31

Despite conflicts between the states and the federal government, the federal-state relationship in the UI system has retained support in the 1990s. While there is an active movement to return training programs and even the public employment service to the states in the form of block grants, the federal-state UI system looks quite secure. The advantages of a highly decentralized UI system with a measure of federal oversight are appealing from both policy and political perspectives at a time when the twin missions of the UI program—providing individual income assistance and macroeconomic stabilization—continue to have wide public backing. Although the balance of responsibilities in the federal-state UI system is apt to fluctuate, the basic structure of the system is likely to remain intact for the foreseeable future. The same cannot be said for other employment and training initiatives. Part of the explanation for this difference may be the strength of the federal-state nature of the UI program.

Judgment as a Source of Disagreement

Even if there were no conflicts of interest in UI, many issues would be difficult to settle to everyone’s satisfaction. Rarely are there matters for which the facts available are completely adequate to answer all the questions involved. Research and data analyses can go far to narrow the areas of uncertainty and dispute that surround specific issues. Yet the research results are not always altogether clear-cut and unqualified. The data and their analyses are not always directly or perfectly relevant to the issue at hand, and the conclusions inferred are not entirely
unequivocal. As has been noted with regard to the work disincentive studies of the 1970s, for example, researchers can differ in their methods and in the types of data used, with varying results. These studies have supplied an idea of the direction and general magnitude of some disincentive effects, but the question remains unresolved as to whether the effects measured are significant enough to warrant specific policy action. The research even makes possible estimates of the consequences of such action through simulation techniques, but here, too, there are limitations because not all the factors that can influence events have been accounted for, or because some factors may change and turn out to be more critical than expected, leading to unanticipated results.

What remains, therefore, is the need to evaluate the implications of the information provided and finally to exercise judgment about the policy action proposed. In making such judgments, people will differ because no one is free from predilections or biases or, stated more positively, because individuals hold disparate values. For example, where to set the weekly UI benefit amount is an issue that involves value judgments. Given that a prime objective of the program is to alleviate hardship during unemployment, the weekly amount should be adequate to satisfy that end. But what is adequate? How is hardship to be measured? Benefit adequacy research has examined various measures of expenditures of the unemployed as the levels to be sustained by the benefit received. What should be included among those expenditures is debatable. Furthermore, for a given definition of expenditures, what proportion of beneficiaries should receive a benefit adequate to sustain them—50 percent? 67 percent? 90 percent? How should the concern about the effects of higher benefit amounts on recipient work incentives be weighed in considering a level to set? How should the effects on costs and taxes be taken into account?

In short, a number of subjective judgments are called into play in deciding weekly benefit amount policy and almost every UI provision. For nearly every feature of the program, multiple choices exist concerning what the policy should be. Each provision adopted by a legislative body usually represents a choice among alternatives, based on the judgment of the majority of the legislators and often achieved through compromise and trade-offs. Controversy need not be a bad or destructive fate for UI as long as reasonable adversaries maintain mutual
respect for their differing judgments. Many objective observers would likely agree that the results can improve and strengthen the program, as they have over the life of UI in the United States.

NOTES

1. See Wandner, Robinson, and Manheimer (1984) for a discussion of UI schemes in developing countries.
2 See the discussion in Breul (1965).
3 Brechling and Laurence (1995) provide an extensive analysis of how experience-rated UI tax systems might deal with the problem of financing permanent as opposed to temporary layoffs.
4. One of the most prominent of these expressions came from President Reagan at a press conference in January 1982, when, in response to a question about the gravity of the current unemployment problem, he noted having recently counted many pages of help-wanted advertisements in the newspaper, implying that there were plenty of jobs available (New York Times, January 20, 1982, p. A-30) A later “explanation” of his comment acknowledged that some of the jobs listed called for skills that many of the unemployed did not have
5. The surveys involved random samples of between 1,000 and 1,500 each time the question was asked. Results of the surveys were provided by the Roper Center at the University of Connecticut.
6 In chapter 8, evidence on the extent to which the experience-rated UI tax system acts to stabilize employment is reviewed.
7. Opposition to government transfer payments may be part of the reason that Blank and Card (1991) found that only about 70 percent of those eligible for UI benefits actually draw them.
8. In February 1995, an attack on UI came from very high in the federal government. Within weeks of being seated as Speaker of the U.S. House of Representatives, Newt Gingrich said, “if you’re not at work, why are we paying you...[unemployment insurance] is not a vacation fund.” He cited UI as an example of a government program that discourages job creation by encouraging out-of-work people to sit and collect money instead of learning new skills (Rice 1995).
9. Similar linkages between unemployment compensation and active employment measures have been forged in other Organization for Economic Co-operation and Development (OECD) countries See Brodsky (1994, pp. 58-59)
10 An excellent overview of the history and philosophy of the insurance concept is given in Malisoff (1961).
11. A similar argument about social security is made by Cohen and Beedon (1994).
12. While the weekly UI benefit is limited because of social adequacy considerations, private supplementary unemployment insurance is available. Workers may purchase—in a fashion similar to credit life and disability insurance on loans—unemployment insurance that guarantees periodic consumer loan payments during unemployment up to a certain duration. This option may represent a significant supplement in a consumer society where virtually everything from homes and cars to groceries and air travel may be purchased on credit.
14. In the United States prior to the 1930s, the only reliable employment data came from the decennial census. The census relied on the gainful worker concept, which excluded unemployment since most of the unemployed held a job at one time or another during the interview year (Levitan, Mangum, and Marshall 1981, p. 77).
15. Blaustein (1981) proposed a type of unemployment assistance as part of a suggested three-tier system of job and income security for workers.

16. Note that the benefits listed in table 1.2 do not include payments for extended or third-tier programs.

17. A further stabilizing influence may be exerted by the UI benefit financing mechanisms. While UI benefit payments increase during recessions, tax payments by employers for those benefits occur gradually over a period ranging between 4 and 24 calendar quarters later. The full benefit repayment burden is not placed on employers during recessionary times.

18. The $700 billion figure for 1993 includes the largest entitlement program, social security old age pensions, which does not means test payments.

19. Striner (1972), who advocated using the Unemployment Trust Fund for training, provides an early comparative review of active labor programs and financing in Europe and the United States. A more recent review is provided by Schmid, Reissert, and Bruche (1992).


23. Part of the present variation in eligibility rules across states has resulted from changes over time in response to the realities of the differing industrial mix of employment and unemployment and the impact of these on benefit payments and UI tax levies.

24. The trends in statutes can be followed in the various revisions to U.S. Department of Labor, Comparison of State Unemployment Insurance Laws.

25. Examples are Gilmore (1960, 1964); and "Another Ripoff?" Sixty Minutes, April 25, 1976.

26. A claimant for unemployment benefits interviewed on the CBS Sixty Minutes program of April 1976, who admitted that he did not seek or want work, a fact he concealed from the state agency when he filed his claim, was disqualified from drawing benefits the morning after the program was shown.


28. Results from the Maryland experiment are to be available in late mid-1997.


30. Nelson (1969, p. 47) states that "at least twenty-three company unemployment-insurance funds, covering approximately 60,000 workers, were in operation at one time or another between 1916 and 1934. There were never more than sixteen plans in effect at one time, and this peak was reached only in 1931."

31. This is the view advanced by Rubin (1983) at the conclusion of his book.
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