Unemployment Insurance, Then and Now, 1935–85

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At the same time that solutions were being sought for the problems of people reaching old age without income and savings in the depressed American economy of the 1930's, another income-maintenance problem was being intensively scrutinized—unemployment among able-bodied workers of all ages. If poverty in old age represented a burden no longer to be accepted, so, too, did the involuntary unemployment of millions of American workers. The Great Depression resulted in job loss for many workers and brought destitution to them and the families who depended on them. Amid controversy about the best way to deal with poverty in old age and with unemployment, the Congress established the old-age and unemployment insurance programs. As with old-age insurance, the unemployment insurance program was incorporated in the legislative package enacted as the Social Security Act of 1935. This article reviews the origins, development, and status of unemployment insurance on its 50th anniversary, and indicates some of the issues still faced by the unemployment insurance system.

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Before the Social Security Act was passed, a variety of plans already in operation were providing benefits for unemployment. Several European countries had established public programs of benefits. Most notably, the English and German systems were studied by many reformers and legislators as potential models for an American program. Domestically, a number of States had considered providing benefits to unemployed workers, but only one—Wisconsin—actually enacted a program, in 1932. In addition, a number of voluntary unemployment compensation schemes were operating in the 1920's and 1930's. They were instituted by forward-looking businesses concerned with stabilizing the economic cycle, including the recurrent layoffs that troubled industry.

The existence of private voluntary plans paying benefits to unemployed workers highlighted the issue of whether or not a public mandatory program should be established. Some of these plans were quite successful for periods of time, but eventually even the larger ones could not continue to pay benefits as the Great Depression deepened. Representatives of many of these plans appeared before Congress to testify about the need for a general unemployment insurance system. Throughout the debates in Congress, however, there continued to be strong advocates for solving the problem of unemployment through voluntary action. Arguments continued to be made also that a public system of unemployment benefits would weaken workers' willingness to work and be detrimental to the economy.

To bolster their views, proponents of a public program could refer to other programs already in operation. Each of the plans already in existence offered insight into some of the issues and pitfalls in establishing a successful public program of unemployment compensation. Many advocates of a public system in the United States, for example, were loath to follow Great Britain's example. That country had established the first successful national compulsory system in 1911. The program that ultimately became law in the United States incorporated some of the English principles of social insurance, especially the conditions under which benefits are payable.[1] But the British system experienced various difficulties because of long periods of severe unemployment. In trying to meet the needs of workers, the government repeatedly liberalized eligibility requirements and extended the potential duration of benefits, encountered severe financial difficulties, and began paying benefits on the basis of need to many workers who were not qualified under the insurance program. Great Britain's experience influenced the determination of the Congress to avoid a "dole" and to avoid any benefit plan that might lead to insolvency of the new system.

The principles incorporated in Wisconsin's 1932 legislation also had pervasive influence on the national program that emerged. The Wisconsin program, drawing on the experience of the States in their workers' compensation laws, emphasized the responsibility of individual employers for unemployment in their firms. This was accomplished through a funding system based on individual employer experience. The Wisconsin emphasis on preventing or minimizing unemployment through employer action was later reflected in the "experience rating" feature of the Federal-State program. Under experience rating, uniform tax rates to fund unemployment benefits may be modified for individual employers who have been responsible for less unemployment than other employers.

Perhaps the most crucial question to be decided about enacting an unemployment insurance program nationally was at what level of government the program would be controlled and operated. Drawing on the experience of some of the European countries and aware of the weakness of the fragmented voluntary programs in the United States, many reformers urged a strong national program under the Federal Government. If they could not have voluntary programs, others preferred State legislation to establish unemployment compensation. But each State hesitated to impose on employers the higher costs entailed in establishing an unemployment insurance program. It was believed that such extra costs might drive employers out of the State or make it less likely for new businesses to enter that State. Hence, through 1934 this fear of the adverse effects of interstate competition kept all States but Wisconsin from passing such a law. Pressure mounted for the Congress to enact legislation. Because of concern that the Supreme Court would declare a national program unconstitutional, a novel arrangement was created under which the States would be given strong incentive by a Federal tax measure to set up their own programs.

The Social Security Act of 1935

Federal Law and Objectives

On August 14, 1935, the Social Security Act was signed. It included the mechanism for establishing an unemployment insurance system in all States. The unemployment insurance provisions of the new law were contained in titles III and IX. A payroll tax on covered employers was established. It was 1 percent of payroll in 1936, 2 percent in 1937, and 3 percent in 1938 and thereafter. However, up to 90 percent of this tax (or 2.7 percent beginning in 1938) could be reduced by contributions that employers paid under an approved State unemployment insurance law. In addition, employers could credit against the 2.7 percent Federal tax any re-

[1] See Edwin E. Witte, **Some Aspects of Unemployment Insurance in the United States**, paper delivered at American Economic Association meeting, "Unemployment Insurance and Relief," Chicago, December 28, 1936.

ductions in the State tax made under an approved State experience rating plan. That is, if the State tax was less than 2.7 percent as a result of reductions allowed employers who laid off fewer workers than other employers, the difference between 2.7 percent and the actual tax rate was also creditable against the Federal tax.

Employers of eight persons or more in at least 20 weeks in a year were subject to the Federal payroll tax, which, in effect, made this size firm the minimum size to be covered. Railroad workers were covered, but in 1938 a separate, completely Federal system of railroad retirement and unemployment insurance was legislated, superseding the Social Security Act coverage. Farm workers, government employees, employees in nonprofit industry or in domestic service, family members of employers, and seamen were the main groups excluded from coverage.

In addition, the Federal law provided broad standards still in effect today for approval of State programs. For example, compensation cannot be denied to any otherwise eligible claimant who refuses to accept new work that violates labor standards (such as work at a subminimum wage). As another condition of approval of a State program, all State tax funds must be deposited in the Federal Unemployment Trust Fund created by the Federal law. These deposits are credited to the State's account and may be withdrawn only to pay unemployment insurance benefits.

Grants are authorized to each State to administer the State unemployment insurance program. To receive these grants, the States are required to meet certain standards of administration, including procedures to pay benefits when due, allowing unemployed workers an appeal procedure if they are denied benefits, and providing information about the operation of the program to the Federal Government. All compensation under the State plan has to be paid through public employment offices or other approved agencies. The State staff administering the program must be employed in accordance with personnel standards on a merit basis.

The unemployment insurance provisions of the Social Security Act established a different system than that enacted for the old-age insurance and later the survivor, disability, and health insurance parts of the law. A tax offset device was used to promote passage of the unemployment insurance laws in all the States. The Federal Government retains an overseer's role in assuring that the States' programs meet certain broad standards of administration and in channeling the collection and disbursal of funds for benefit payments. But the States operate their programs directly and they determine eligibility conditions, the waiting period to receive benefits, benefit amounts, minimum and maximum benefit levels, duration of benefits, disqualifications, and other administrative matters.

What are the objectives of this program created by the Social Security Act? On the program's twentieth anniversary in 1955, the Secretary of Labor published this list:[2] (1) Unemployment insurance is intended to offer workers income maintenance during periods of unemployment due to lack of work, providing partial wage replacement as a matter of right; (2) it is to help maintain purchasing power and to stabilize the economy; and (3) it is to help prevent dispersal of the employer's trained labor force, the sacrifice of skills, and the breakdown of labor standards during temporary unemployment.

Translating these general objectives into more specific goals, the Secretary recommended as Federal policy that unemployment insurance should cover as far as feasible all workers subject to the risk of involuntary unemployment; that workers should qualify for benefits if they have had recent and substantial attachment to the labor force; that weekly benefits should be sufficient to cover nondeferrable expenses (a benefit of at least 50 percent of gross wages); that the duration should be sufficient to protect workers through periods of temporary unemployment (at least 26 weeks for all eligible workers); that the disqualification provisions should assure that claimants be involuntarily unemployed through no fault of theirs and that they be able and available for work, but the provisions should not be punitive; that the States should facilitate the payment of benefits to workers who move from one State to another; that financing should be sufficient to insure the payment of benefits in economic downturns, increasing reserves in good years; and that opportunities for the reemployment of claimants should be increased through the coordination of efforts with the Employment Service.

State Laws

The Social Security Act instituted broad guidelines for the States to follow. The enacted State laws matched the minimum requirements and, in many instances, exceeded them. In terms of the workers to be protected, table 1 shows that, as of 1938, 31 States and the territory of Alaska covered only firms with eight employees or more in at least 20 weeks in a year, as called for by the Federal law. The other 20 jurisdictions covered more firms (and workers) than required—including eight States, the District of Columbia, and the territory of Hawaii, which protected workers in firms with one employee or more, generally in at least 20 weeks. Other exclusions from coverage, in most instances, were the same under State law as under Federal law (agricultural workers and government workers, for example).

When the laws were first enacted, the State legislators

[2] **Employment Security Review**, Bureau of Employment Security, Department of Labor, August 1955.

Table 1.—State unemployment insurance laws in effect May 1, 1938, and January 1, 1985, by State and selected benefit provisions

State	May 1, 1938			January 1, 1985		
	Waiting period (in weeks)	Maximum benefits payable		Waiting period (in weeks)	Maximum benefits payable	
		Weekly amount	Number of weeks		Weekly amount	Number of weeks
Alabama	3	$15	20	0	$120	26
Alaska	2	15	16	1	188 D	[1] 26
Arizona	2	15	14	1	115	26
Arkansas	2	15	16	1	154 A	26
California	4	15	20	1	166	[1] 26
Colorado	2	15	16	1	206 A	26
Connecticut	2	15	13	0	180 A D	[1] 26 U
Delaware	2	15	13	0	165 A	26
District of Columbia	3	15 D	26.6	1	206 D	26
Florida	3	15	16	1	150	26
Georgia	2	15	16	[2] 1	125	26
Hawaii	3	15	15	1	194 A	[1] 26 U
Idaho	3	15	20	1	173 A	26
Illinois	3	15	16	1	161 A D	26 U
Indiana	2	15	15	1	84 D	26
Iowa	2	15	15	[2] 1	143 A D	26
Kansas	2	15	[3] 16	1	175 A	26
Kentucky	3	15	15	0	140 A	26
Louisiana	4	15	25	1	205 A	26
Maine	2	15	16	1	139 A D	26
Maryland	2	15	16	0	175 D	26 U
Massachusetts	3	15	28.8 +	1	196 A D	30
Michigan	3	16	16	0	197 D	26
Minnesota	2	15	16	[4] 1	198 A	26
Mississippi	2	15	14	1	115	26
Missouri	3	15	12	[4] 1	120	26
Montana	3	15	16	1	171 A	26
Nebraska	2	15	16	1	120	26
Nevada	2	15	18	0	162 A	26
New Hampshire	3	15	16	0	141	26 U
New Jersey	2	15	16	[4] 1	203 A D	26
New Mexico	2	15	16	1	150 A	26
New York	3	15	16	1	180	26 U
North Carolina	2	15	16	1	167 A	26
North Dakota	2	15	16	1	185 A	26
Ohio	3	15	16 U	[4] 1	147 A D	26
Oklahoma	2	15	16	1	197 A	26
Oregon	2	15	16	1	204 A	26
Pennsylvania	3	15	13	1	224 A D	26
Rhode Island	2	15	20	1	174 A D	26
South Carolina	2	15	22.6	1	125 A	26
South Dakota	3	15	14	1	129 A	26
Tennessee	3	15	16	1	120	26
Texas	2	15	16	[4] 1	189 A	26
Utah	2	15	16	1	186 A	26
Vermont	3	15	14	1	146 A	26 U
Virginia	2	15	16	0	150	26
Washington	2	15	16	1	185 A	30
West Virginia	2	15	12	1	225 A	28 U
Wisconsin	3	15	20	0	196 A	26
Wyoming	2	18	14	1	183 A	26

[1] Benefits extended by 50 percent under State program when unemployment in State reaches specified level.

[2] In Georgia, the waiting week is waived for claimants unemployed through no fault of their own; in Iowa, the waiting week will be repealed on January 1 of the first calendar year for which a contribution rate table other than the highest is in effect.

[3] For beneficiary at maximum weekly benefit amount and maximum qualifying wages (8 percent of wages is credited to the account).

[4] Waiting week becomes payable: after receiving benefits for 9 weeks in Missouri; 3 weeks in New Jersey, Ohio (after 1985), and Texas; and after 4 weeks if reemployed full-time in Minnesota.

Note: A denotes that the maximum automatically increases each year with rising wages; D denotes dependents' allowance also payable, but in the District of Columbia, Maryland, and New Jersey, the same maximum applies with or without dependents; U denotes uniform maximum applies to all beneficiaries.

Source: **Comparison of State Unemployment Insurance Laws**, Department of Labor, Unemployment Insurance Service, 1938 and 1985.

were committed to establishing programs that would be fiscally sound and would not provide more in benefits than could be prudently financed. They first provided for a 2.7 percent tax rate on employers to build up reserves as required by the Social Security Act and they established conservative benefit provisions. All the laws provided that after the unemployment began, a worker who met the monetary qualification and eligibility re-

quirements [3] could start drawing benefits only after a 2-4 week waiting period. There was widespread agreement among the States that workers should receive a benefit equal to about 50 percent of their recent earnings. This goal was reflected in the benefit formulas of all the States. However, because of concern about excessive costs and because of a desire to limit the extent of benefits provided to higher paid workers, weekly maximums were also established in each State ($15 in all but two). The weekly maximum benefit, of course, limits the attainment of a 50-percent replacement rate to individuals whose earnings were below certain wage levels.

As shown in table 1, the potential maximum duration of benefits varied considerably, ranging from 12 to 28.8+ weeks. But four-fifths of these maximums were for 16 weeks or less. Further, duration was generally fixed by a formula that varied the number of weeks allowed in proportion to the amount of previous earnings or employment. Thus, in a State with a specified maximum, a substantial number of claimants were eligible for less than the maximum number of weeks.

Experience Under the Program

In 1938, when all the State laws were in place and benefit payments began in most of them, 20 million workers were covered by the program nationally. This number represented less than two-thirds of employed wage-and-salary workers in that year. From then until 1985, the labor force has grown and so has the extent of statutory protection—to 92.5 million workers covered (96 percent of wage-and-salary workers) in January 1985. Thus, aside from some workers in very small firms and in agricultural work, and some specialized occupational groups such as elected officials and persons who work for family members, almost all wage-and-salary workers are now covered by the unemployment insurance laws.

In 1940, the second year for which benefits were paid in all States, 5.2 million workers received an average of $10.56 per week for almost 10 weeks. Altogether, $519 million was paid under the State programs in that year. By 1982, the year with the highest unemployment insurance expenditures, $20.6 billion was paid by the States to 11.6 million workers (excluding amounts under extended benefits programs). In that year, an average beneficiary received $119.39 per week for almost 16 weeks. Most recently, as the economy has improved, the total amount of benefits has declined: The $1.0 billion in benefits paid for August 1984 represented a $12 billion annual rate in benefit expenditures.

[3] Monetary qualification requirements are specified amounts of work or earnings to establish that the worker had substantial and recent employment. Eligibility requirements pertain to the claimant's being able to work and available for employment, being involuntarily unemployed, and meeting other tests of a valid claim.

In general, the basic structure of unemployment insurance continues today much the same as when it originally was enacted 50 years ago: Joint Federal-State administration, weekly benefits of about 50 percent of a worker's wage (up to a stated maximum) for workers with recent work experience, protection for temporary periods with a set maximum duration, program financing through a payroll tax on employers, and experience rated tax schedules. Nevertheless, unemployment insurance has also changed. As indicated, the proportion of workers with this type of income-maintenance protection has grown to a point where coverage is nearly complete.[4] The scope of protection has been enhanced in a major way by the provision for automatic increases in weekly benefit maximums to account for rising wages in about two-thirds of the States and through the extension of the maximum potential duration of benefits under the regular program and the establishment of extended benefit provisions.

The Federal agency originally responsible for overseeing the operation of the State programs was the Social Security Board, which also administered the old-age insurance and income-support provisions of the law. In August 1949, the Federal responsibility was transferred to the Department of Labor, where it remains. A number of the financing provisions also have been changed from those in the original program—namely, a much wider range of payroll tax rates on employers, but with a corresponding cutback from taxing all covered payrolls to taxing up to a set maximum (currently $7,000 per worker under Federal requirements). Further, when they first were enacted, 10 State laws called for employee contributions as well as employer contributions. By 1940, only five States required employee contributions, and since 1955 only three have retained this provision. These changes resulted from a number of amendments to the Federal law as well as changes in the State programs. A discussion of some of the more significant legislative changes follows.

Federal Developments

Coverage. The first changes in coverage under Federal law were the new restrictions imposed in 1939 and 1948. By broadening the definitions of the groups already excluded, still more farm workers, employees of nonprofit organizations, insurance agents, commission salesmen, and certain employees under the "master-servant" definition in common law were removed from covered employment. The 1939 amendments did add certain government instrumentalities to coverage, including bank members under the Federal reserve system.

[4] Some persons might argue that certain groups traditionally not considered insurable under unemployment insurance should be included, such as new labor-market entrants.

The size-of-firm restriction was eliminated in two steps: The 1954 amendments reduced the restriction to four workers or more in 20 weeks, and the 1970 amendments extended the Federal tax to all firms with one worker or more in 20 weeks or with a quarterly payroll of $1,500 or more. All State laws cover at least firms of this size, and currently about one-third provide even broader coverage. For example, some laws specify coverage for firms of one worker or more at any time.

The other major extension of coverage was the addition of specific occupational or industrial groups of workers. The 1954 amendments provided a separate program to cover Federal civilian employees (Unemployment Compensation for Federal Employees—UCFE). Benefits are the same as for other workers in the State where the employee last worked, and claims are filed through State offices.

The UCFE program is financed directly by the Federal Government. Military personnel separated from active duty had been provided unemployment benefits through temporary programs enacted in 1944 and 1952. A permanent program for those benefits was established in 1958 (Unemployment Compensation for Ex-Servicemen—UCX). Benefit amounts and duration were governed by the law of the State in which the ex-serviceman filed a claim. This program has been amended and currently provides limited benefits: A maximum of 13 weeks duration, after a waiting period of 4 weeks following separation from the military, for personnel discharged (1) at the completion of a first full term of active duty or (2) for the convenience of the Government or under certain personal or family hardship conditions.

The next major expansion of coverage after 1954 was enacted in 1970 (effective in 1972) when, in addition to expanding coverage to firms with one employee or more, coverage was mandated for specified nonprofit organizations with four employees or more, State institutions of higher education and State hospitals, agricultural processing firms, and work performed overseas by American citizens for American employers. In addition, definitional changes in the term "employee" added agent-drivers, outside salesmen, and others who had not been covered under the more restrictive previously used common law definition of employee.

The last significant Federal addition to the groups of workers protected was incorporated in the 1976 amendments (effective in 1978). About 8.6 million jobs were added to the 72.4 million already covered, including: Farm employment (in operations with a payroll of at least $20,000 in a quarter or 10 employees in 20 weeks), domestic employment in private households (where at least $1,000 in wages was paid in a recent calendar quarter), State and local government employment, and employment in nonprofit elementary and secondary schools (with four employees or more in 20 weeks).

Other Federal coverage provisions have been enacted over the years affecting small groups of workers. Seamen have been covered to different degrees since 1946 but, as recently as 1984, crews in certain small fishing vessels were temporarily excluded.

Duration of benefits. Since the inception of the program, more major Federal legislation on unemployment insurance has pertained to the duration of benefits than to any other topic. The large number of temporary programs extending duration of benefits and the permanent program established in 1970 and amended many times since then reflect both the importance of this problem and the difficulty that unemployment insurance programs have in dealing with it.

No Federal changes were made in duration provisions through 1957, even though the economy experienced recessions in 1948-49 and 1953-54. States had improved the duration provisions of their programs considerably since 1938. Most States provided a maximum of 16 weeks or less in 1938, and variable duration provisions in all but one State meant that many claimants were entitled to even shorter duration than the stated maximum. By 1948, the maximum duration in the large majority of States was 20-26 weeks, and by the mid-1950's more than half the States had maximums of at least 26 weeks. By 1958, however, during the third postwar recession, unemployment reached 7.4 percent nationally, the highest level since before World War II. The Congress responded by passing the Temporary Unemployment Compensation Act of 1958. This law offered interest-free loans to States that increased by 50 percent the duration of benefits to unemployed workers who exhausted regular program benefits. Seventeen States participated in this voluntary program. (Five States enacted their own programs and also paid extended benefits.)

In the next downturn, the first mandatory extension of benefits applicable to all States was legislated: The Temporary Extended Unemployment Compensation Act of 1961. This law authorized additional weeks of benefit payments to individuals who had exhausted their benefits. The extended benefit period could equal up to 50 percent of the regular program entitlement period as long as it did not exceed 13 weeks or a combined maximum of 39 weeks in conjunction with the regular program benefit period. The extended benefits were funded from a temporary addition to the Federal payroll tax on employers.

Throughout the 1960's, the Congress considered proposals to establish a permanent program of extended benefits, which was, however, not enacted during that prosperous decade. The Extended Unemployment Compensation Act of 1970 instituted a mandatory permanent program that paid extended benefits (EB) nationally or in individual States with high unemployment, according to whether specified unemployment

rates were reached. The number of extended benefit weeks again was established at the lesser of either half of the worker's regular program duration or 13 weeks, with an overall combined maximum of 39 weeks. The Federal Government and the States shared equally in the financing of these benefits through increases in their respective unemployment insurance payroll taxes.

Even with this permanent program in place, through 1985 more than a dozen Federal laws have been passed concerning extended benefits. Many of these attempted to fine tune the trigger provisions of the EB program as unemployment conditions changed. Others added temporary extensions on top of the permanent benefit provisions. As many as 65 weeks of benefits were available to an individual under the Emergency Compensation and Special Unemployment Assistance Extension Act of 1975, the longest extension ever provided of these various benefits. In addition, special assistance was provided in 1974 and 1975 to groups not protected under the regular program. (Many of these workers were included in the regular program by the 1976 coverage amendments.)

In the 1980's, two major developments have occurred. The 1981 amendments modified the permanent EB program as follows:

(1) The national trigger was rescinded so that EB is payable only in individual States meeting the State trigger requirement.
(2) The State trigger, effective September 25, 1982, is an insured unemployment rate of 5 percent rather than the 4-percent rate previously used. (The rate must also be at least 120 percent of the average rate of the previous 2 years.)
(3) The States can provide EB at their option, even if the current insured unemployment rate is not at least 120 percent of the average rate for the corresponding rate of the previous 2 years, as long as the current rate is 6 percent (previously 5 percent).

Most recently, a new temporary program of extended benefits, Federal Supplemental Compensation, was enacted, in September 1982. This program added a varying number of weeks of benefits (up to 14, in the most recent amendments of 1983) for workers who exhausted regular program benefits and EB, if they had been eligible for them. This program ended in March 1985.

Starting in 1958, the various Federal enactments over the years to supplement regular program benefits have added a major new facet to the original 1935 law. However, it is also evident from the many legislative changes in the 1970's and through the early 1980's that, in providing these extended payments, the program continues to evolve.

Financing. The first important change in financing unemployment insurance came in 1939. At that time, the Federal unemployment tax base was changed from total covered wages to the first $3,000 of covered wages in order to match the tax (and benefit) base under the old-age insurance provisions. When the cap on the wage base was legislated, it had very little effect because most workers earned less than this amount. However, as wages rose sharply, the $3,000 base significantly changed the distribution of unemployment insurance taxes in various industries and areas. Pressure to update the base resulted in amendments raising the Federal tax base to $4,200 in 1970 (effective in 1972), to $6,000 in 1976 (effective in 1978), and to $7,000 in 1982 (effective in 1983). Under the $7,000 Federal base, about 43 percent of all covered payrolls were taxable in 1983. Of course, the States can, and many have, enacted higher tax bases. As of January 1985, 32 States had a higher tax base than the Federal level.

The Federal tax rate has been changed a number of times since 1935. The first increase was from 3.0 percent to 3.1 percent in 1961, with the maximum offset credit remaining at 2.7 percent. This change left an additional 0.1 percent for the net Federal tax, to be used to defray the growing administrative expenses of the system and to replenish a loan fund established earlier to make advances available to the States (as needed for benefit payments). Subsequently, the Federal rate has been raised several times, sometimes on a temporary basis, and, in most cases, to provide for the costs of extended benefit programs. Effective January 1, 1985, the Federal tax rate became 6.2 percent, including a 0.2-percent temporary levy that will stay in effect until general revenue advances made to finance the Federal share of extended benefits in recent years have been repaid. The maximum offset credit for employers is 5.4 percent, so that the net Federal tax is 0.6 percent (plus the temporary 0.2 percent tax).

The Federal law has been changed in other ways that affect program financing. The tax credit granted to employers for experience rating could begin only after 3 years of experience under the original legislation. In 1954, this period was shortened to 1 year, and subsequently the law was modified again to permit the full tax credit without any waiting period to employers taking over already established businesses. Employer credits are affected by the Federal legislation concerning delinquent repayment of loans made to the States.

Federal standards. Major changes in Federal rules concerning State operations were enacted in the 1970 amendments. At that time, States were prohibited from: (1) paying benefits to a claimant in a second successive benefit year unless the claimant had intervening employment; (2) totally eliminating benefit rights except for misconduct in connection with the job, fraud, or disqualifying income, or from reducing benefits to workers from another State; (3) denying benefits of claimants taking approved training on the grounds of lack of availability for work or work refusal; and (4)

refusing to participate in arrangements for determining benefits based on combining wages in more than one State.

Under legislation enacted from 1976 through 1983, other Federal requirements have been established concerning the denial of benefits under certain circumstances (for example, for school employees between academic years); an offset of unemployment insurance payments by the amount of retirement benefits; [5] and coordination by State unemployment insurance agencies with State child support enforcement agencies to ensure the payment of child support.

A number of changes were instituted over the years besides those related to coverage, benefit duration, financing, and Federal standards. One of these that subsequently has also had legislative effects on the social security program (in 1983) was the taxation of unemployment insurance benefits. Under the Federal laws of 1978 and 1982, unemployment insurance benefits were made taxable under Federal income tax. Currently, a taxpayer must include in gross income for income tax purposes the lesser of the amount of unemployment benefits paid or half the excess of adjusted gross income plus unemployment benefits plus excludable disability income in excess of $12,000 (for single taxpayers) or $18,000 (for married taxpayers filing jointly).

State Programs

Every year a number of changes occur in State laws, including some to conform with Federal requirements. Throughout the past 50 years, the States truly have served as a laboratory for trying the many different ideas for operating an unemployment insurance system. In almost every aspect, the States have differed in their approach—on having benefit allowances for dependents; establishing flexible maximum benefit provisions; providing uniform or variable maximum potential duration; disqualifying claimants involved in labor disputes; basing benefit formulas on weekly, quarterly, or annual wage records; maintaining employer tax contributions in separate employer accounts or a statewide pool; or allowing claims by mail, to name a few.

Except for a limited number of Federal requirements, the States have had primary or exclusive responsibility for most facets of unemployment insurance. As can be seen from table 1, the State programs have converged in certain respects over the years. In 1938, waiting period requirements varied considerably; by 1985, four-fifths of the States required a 1-week uncompensated period before unemployment benefits began. Similarly, maximum potential duration has reached 26 weeks in almost all States. Both these provisions represent a greater degree of protection for unemployed workers.

There have been marked changes in the extent to which the States provide the same duration ("uniform duration") to all claimants who qualify for benefits, rather than provide duration that varies according to the worker's most recent length of employment. Only one State had uniform maximum duration in 1938. By 1941, 16 States provided uniform duration. But the trend since then clearly has been away from uniform duration provisions, reflecting a preference for relating the extent of protection to the extent of recent labor-force experience. Currently, eight States have uniform duration.

All the States have raised benefit maximums greatly but by considerably different amounts over the years. All but two States provided a maximum weekly benefit of $15 in 1938; all the States provided a range of maximums from $84 to $225 by 1985. The States generally still adhere to the principle of paying a weekly benefit that replaces about half of the worker's wage. However, the benefit formulas vary considerably in implementing this general goal. Some States have a weighted formula to give lower paid workers a somewhat higher proportion of lost earnings; others provide an allowance for dependents.

The most noteworthy development in the State laws dealing with benefit amounts was the adoption of flexible maximum weekly benefit provisions—that is, provisions that automatically raise the maximum, usually as the State average weekly wage rises. In 1949, only Kansas had such a provision. By 1985, two-thirds of the States had flexible maximums. This type of provision keeps benefit levels current as workers' wages increase. In States that must rely on ad hoc statutory increases, the maximum benefit tends to lag behind wages. However, even in States with flexible maximums, many beneficiaries are entitled to benefits that represent less than half their wages. This discrepancy results when the relationship between the maximum benefit and the State average weekly wage in covered employment is set too low (in eight States with flexible maximums, for example, the maximum benefit is set at less than 60 percent of the State's covered wage). Further, as of January 1985, seven States had frozen their maximum benefit amounts, temporarily setting aside the automatic provision.

The question of disqualification from benefits is another area in which the States have acted with great diversity—both in defining what types of circumstances should result in disqualification and in determining the appropriate manner of reducing (or eliminating) benefits because of specified disqualifying acts. More important, in certain respects, the State laws have become more stringent with the passage of time. In the first 25

[5] The unemployment benefit is reduced dollar-for-dollar by receipt of a private pension to the extent that the pension is provided by the same employer who provided the unemployment insurance coverage, and that work counted toward the pension rights. Social security retirement insurance benefits also serve to reduce the unemployment benefit. In figuring the reduction, States can take into account the effect of employee contributions on the pension or social security benefit.

years of the program, "The causes for which benefits are denied have multiplied and the periods of disqualification have been made more severe." [6]

Since 1960, the same patterns have continued. For refusal to accept suitable work, for instance, just 15 States imposed a disqualification for the duration of unemployment in January 1960 (as opposed to disqualification for a specified fixed or variable period), but 40 States imposed this disqualification in January 1985. Similarly, for voluntarily leaving the job or for discharge for misconduct, the number of States disqualifying a claimant for the duration of his unemployment rose significantly:

Date	Voluntarily leaving	Misconduct
January 1960	17	10
January 1985	47	39

These changes and other similar changes represent an attempt to discourage inappropriate use of the unemployment insurance program and to conserve funds, especially during periods of high unemployment when large amounts of benefits are being paid.

Experience rating has become a basic part of the unemployment insurance financing structure to maximize employment stabilization efforts by employers. Under experience rating, employers who maintain a stable work force are assigned favorable tax rates compared with the rates of other employers. Table 2 indicates a few of the trends in experience rating over the years. First, although many States have encountered difficulties in financing benefits, especially during recessions, some States continue to allow a tax rate as low as zero to employers under the most favorable schedule (11 States in 1985). The conservative approach used in financing benefits early in the history of the program is discernible from the fact that, even under the most favorable schedule, the majority of States imposed a rate of at least 0.9 percent in 1937, but the minimum rate in almost all States had declined to 0.5 percent or less in 1960 and remained at that level in 1985. The maximum tax rates rose sharply between 1960 and 1985 for employers with unfavorable experience. But this change is largely a result of the federally mandated increase in the Federal tax instituted in 1985 (raising the Federal tax from 3.5 percent to 6.2 percent). One result of the most recent changes is that the range of experience rates has been expanded, allowing the States to better match employers' experience with their tax rate.

[6] R. Gordon Wagenet, "Twenty-Five Years of Unemployment Insurance in the United States," **Social Security Bulletin**, August 1960, page 56.

Table 2.—Number of States with specified minimum and maximum contribution rates in 1937, 1960, and 1985

Minimum rate (most favorable schedule)	Number of States			Maximum rate (least favorable schedule)	Number of States		
	1937	1960	1985		1937	1960	1985
Total [1]	40	48	50	Total [1]	37	50	51
0	12	15	11	2.7	10	34	0
0.01-0.1	0	16	17	2.9-4.0	27	15	0
0.11-0.2	0	3	3	4.2-5.2	0	1	7
0.21-0.3	0	6	7	5.4	0	0	14
0.4-0.5	1	6	8	5.5-6.0	0	0	6
0.6-0.8	0	1	1	6.1-7.0	0	0	14
0.9	13	0	1	7.1-8.0	0	0	3
1.0 or more	14	1	2	8.1 or more	0	0	7

[1] Includes District of Columbia. States not included did not provide variable rates according to individual employer experience (11 States in 1937; 1 in 1960), or provided variable rates other than through specification in the law.

Source: **Comparison of State Unemployment Insurance Laws**, Department of Labor, Unemployment Insurance Service, 1960 and 1985, and **Employment Security Review**, Bureau of Employment Security, Department of Labor, August 1955.

As indicated above, a number of States have raised their taxable wage base above that required by Federal law. In the early years, few States exceeded the Federal requirement. As wages rose by substantial amounts, however, and the Federal bases remained at low levels, more and more States took the initiative and revised their tax base. By 1970, 27 States had legislated higher bases than the original $3,000 Federal base still in effect. The growing pressure that higher costs exerted on the system during periods of high unemployment (and hence high benefit payments) has induced 32 States to raise their tax base above the Federal level, even though the Federal amount has been increased a few times, reaching $7,000 by 1985.

Current Issues

How has the unemployment insurance program met its goals over the past 50 years? Clearly, in broad terms unemployment insurance has developed into a valuable segment of the Nation's income-maintenance structure by providing income to replace lost wages to the unemployed through more than 2,000 local offices. In transferring large amounts of money to workers and their families during economic downturns, it has been a significant force in stabilizing the economy.[7] In providing a readily available source of replacement of wages to unemployed workers, it has helped employers by preventing dispersal of their trained labor force, the loss of skills, and the breakdown of labor standards during periods of temporary unemployment.

The rate of progress has varied for different aspects of the protection offered by the unemployment insurance program. Extension of coverage has been almost complete, in contrast to the moderate scope of the program mandated in the Social Security Act. Waiting periods have been reduced and benefit duration has been extended since the early days of the program.

[7] It has been cited as second only to the Federal income tax as the major economic stabilizer of the economy. See George M. von Furstenberg, "Stabilization Characteristics of Unemployment Insurance," **Industrial and Labor Relations Review**, April 1976, page 364.

And yet, some of the current questions about the program point to inconsistencies inherent in the different goals of the system. The adequacy of the weekly benefit amount is an important case in point. One long-accepted goal of the program has been to provide a benefit/wage-replacement rate of 50 percent to the great majority of unemployment insurance beneficiaries. Almost all the statutory formulas call for this level of benefits. On the other hand, much concern has been expressed—especially in recent years—about the disincentive effects of unemployment insurance benefits on a worker's motivation to return speedily to work. "Considerable empirical evidence supports the conclusion that higher replacement rates induce longer spells of insured unemployment when unemployment is low." [8] This effect might signify that benefits are sufficiently high to produce "a disincentive to return to work or an opportunity for more intensive job search efforts and ultimately better matching of workers and jobs." [9]

These conflicting concerns probably have influenced the trends in statutory benefits. The maximum weekly benefit amount is an indicator of the adequacy of benefits. For the States' 50-percent replacement goal to be achieved, the maximum must be set high enough to prevent too many workers from having their benefits cut off by the maximum rather than having them determined by the formula that would pay 50 percent of the worker's wage. It has been estimated that the State maximum weekly benefit amount should be almost two-thirds of the State average covered wage to ensure that the great majority of beneficiaries receive a benefit replacing 50 percent of their wage.[10]

In the tabulation in the next column, the average of State maximum weekly benefit amounts is shown as a percentage of wages in covered employment for several periods. The States have increased weekly statutory maximum benefits many times over the decades. But the data show that the ratio of the average State maximum weekly benefit amount to the average weekly wage in covered employment nationally (1) was highest at the beginning of the program, (2) has improved gradually from immediately after World War II, and (3) is still well under two-thirds. Thus, it can be expected that under current laws many beneficiaries do not receive a benefit equal to half their wage.[11]

[8] Bruce Vavrichek, **Promoting Employment and Maintaining Incomes with Unemployment Insurance**, Congressional Budget Office, March 1985, page 21.

[9] National Commission on Unemployment Compensation, **Unemployment Compensation: Final Report**, July 1980, page 40.

[10] William Haber and Merrill Murray, **Unemployment Insurance in the American Economy**, Richard D. Irwin, Inc., 1966, page 184.

[11] Much available literature focuses on the adequacy of unemployment insurance benefits, including such complicated issues as whether or not a worker's benefit should be related to some measure of "net" wages and, if so, whether fringe benefits should also be counted. See, for example, **Unemployment Compensation Studies and Research**, National Commission on Unemployment Compensation, vol. 1, July 1980.

As of—	Average statutory maximum weekly benefit amount [1]	Average (gross) weekly wage in covered employment [2]	Benefit/wage ratio (percent)
May 1, 1938	$15.08	$25.36	59.5
September 1, 1947	21.02	51.59	40.7
January 1, 1960	38.43	90.90	42.3
July 2, 1972	66.51	155.12	42.9
January 6, 1985	169.40	[3] 348.69	48.6

[1] Weighted by covered employment in each State.

[2] For calendar year including or immediately preceding effective date of statutory maximum benefit amount.

[3] Preliminary data.

What many persons consider the most intractable and most important issue in unemployment insurance today is that of the appropriate potential duration of benefit payments. The problem represents a conflict between two program premises: (a) The goal of paying benefits for a temporary—that is, limited—period of unemployment, and (b) the need for providing income maintenance to individual workers experiencing involuntary long-term unemployment during periods of high unemployment. Realization of the latter goal helps fulfill the goal of stabilizing the economy.

As the present system evolved, three legislative patterns developed concerning duration of benefits. First, the number of weeks of benefits allowed under regular State programs increased substantially and stabilized at 26 weeks as a typical maximum amount for workers with substantial work experience before a period of unemployment. Second, despite the program objective stated through the mid-1950's—that benefit duration should be at least 26 weeks for all claimants who qualify for benefits—the States have moved in a different direction since 1941. All but eight States now vary potential duration—from 4 weeks to 26 weeks (except for a 28-week maximum in Washington)—by the extent of previous work experience. Variable duration provides some limited degree of protection even to workers who have not had stable full-time employment. Third, some States, and, in 1970, all States (under Federal law), added a supplementary set of benefits to regular program duration. This extended benefit feature for periods of high unemployment continues to be re-examined. The Congress has modified the duration provisions to meet the needs of the unemployed in succeeding business cycles, which have been accompanied by different patterns of unemployment.

It may be that still untried approaches will be considered in the future. One comprehensive alternative to the present system, for example, has been published by the Upjohn Institute for Employment Research, for many years a leading private research organization on employment security programs. This proposal concentrates on tailoring unemployment insurance to the

economic circumstances of the worker rather than of the economy. It presents a three-tier duration system, totaling 39 weeks of benefits. Each succeeding, 13-week tier of benefits would be available only if the claimant satisfied more stringent qualifying requirements at each stage, rather than on the basis of changing economic conditions as in the current EB program. The three-tier program would be followed by a new permanent special assistance program that would extend benefits on the basis of need after workers can no longer qualify for unemployment insurance benefits.[12]

As already indicated, substantial improvements to adequately finance the program have been made in recent years. But it is also evident that additional steps are necessary if the costs of unemployment insurance benefits in future economic downturns are to be provided for in an orderly, planned-for fashion rather than through ad hoc emergency legislation. The need for improving this part of the system was highlighted by the National Commission on Unemployment Compensation, which recommended a number of ways that the Federal law and State laws should be amended to strengthen the funding of the program.[13] Their recommendations included proposals to raise the taxable wage base and establish a flexible level to rise as wages increase; strengthen requirements for borrowing from the loan fund; provide the States with protection against unusually heavy benefit costs to maintain State solvency; eliminate zero minimum tax rates and establish maximum rates in terms of anticipated benefit costs; and ensure effective charging of all benefits in fund replacement provisions of solvency arrangements.

These are a few of the issues that still need to be resolved in the area of unemployment insurance. Other facets of the program such as administration, partial unemployment, taxation of benefits, and disqualifications have been addressed in recent years and continue to receive considerable attention from policymakers and legislators. Because unemployment insurance is part of a dynamic economic system, it will always have to adjust and adapt to new challenges and new problems. But, based on the experience of the past 50 years, it can be predicted without doubt that the system will continue to make the changes needed to maintain its role as one of the Nation's major income-maintenance programs.

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[12] See Saul J. Blaustein, **Job and Income Security for Unemployed Workers**, W. E. Upjohn Institute for Employment Research, Kalamazoo, Mich., 1981.

[13] **Unemployment Compensation: Final Report**, op. cit., pages 2 and 3.