

# Introduction\*

WILLIAM H. WANDEL†

Unemployment compensation is the term commonly used to describe the form of social security designed to protect workers against the complete loss of income when they do not have work and are unable to get suitable work because it is not available. Because it can provide compensation payments only to those who suffer a wage *loss* because of unemployment, it can benefit only those who have had a substantial "attachment to the labor market," that is, a history of working for an employer, are currently involuntarily unemployed, and are currently available for work.

The need for unemployment compensation rests on two bases: the dependence of individuals on current earnings and the persistent character of unemployment in a free economy. As countries advance in industry and commerce, a progressively higher proportion of the population becomes dependent for its living on earnings from the sale of its labor to others. For such, when lay-offs occur, income ceases. And in a free economy, even in periods of prosperity and "full employment," some unemployment is inevitable because technological changes are always requiring some adjustment in the labor force, some businesses are affected by the weather, the seasons, changes in styles and in patterns of consumer purchasing, and because most employers are alert to make adjustments in their work force which will increase production but may also create unemployment. The resulting unemployment is imposed on the individual worker by forces beyond his control and commonly fall upon him with crushing impact. The serious social and economic consequences of distress, exhaustion of savings, impairment of health and morale, resort to relief, and the general lowering of consumer purchasing power extend beyond the individual to the local, State, and national community.

The history of unemployment compensation extends back to the middle of the 19th century when trade unions had plans to pay benefits to their unemployed members. Around the turn of the century, many European cities established voluntary unemployment insurance plans and prior to World War I many of these cities adopted the "Ghent system" of municipal subsidies to trade union funds. The first national compulsory system was adopted by

---

\* The opinions expressed in this article are those of the author and do not necessarily reflect the official views of the Federal Security Agency.

† Chief, Division of Program Standards, Bureau of Employment Security, Social Security Administration, Federal Security Agency.

Great Britain in 1911. Now most foreign countries have systems of unemployment insurance.

In the United States, unemployment compensation is frequently considered to be an outgrowth of the Great Depression. However, as in Europe, even in the 19th century there had been several trade union plans for unemployment benefits. In addition, in this century, some companies developed plans for stabilizing employment and providing unemployment benefits but the number of individuals protected by either the union or company plans never exceeded 100,000. Efforts to provide for unemployment compensation by legislation began in Massachusetts in 1916. Bills were introduced in many State legislatures in 1920-1922 and in many more after the onset of the depression of the early thirties. The only State law enacted in this period was that of Wisconsin, in 1932, but its effective date was postponed until 1936. Bills had also been considered by Congress at various times after 1916 but most Congressional concern was shown after 1928. Unemployment after 1929 became so widespread as to identify it clearly as a problem not responsive to simple local treatment but one requiring national action. This action was first in the form of programs to provide for needy persons through cash payments administered on a relief basis or through compensation for work under Federal work programs. Such relief and work programs were of an emergency character and required millions of people to be subjected to a means test in order to obtain the basic necessities of life. It became apparent that the need for providing for the unemployed through a program that would be permanent and in keeping with the dignity of American workers could only be met by an unemployment compensation program. At the same time, while many States were seriously considering the adoption of unemployment compensation laws, perhaps the most important obstacle encountered was the argument that any State which enacted an unemployment compensation law thereby handicapped its employers in interstate markets by burdening them with costs their competitors in other States were not required to meet. Federal action was required to remove this obstacle.

In 1934, President Roosevelt created the Committee on Economic Security. Its recommendations were reflected in bills introduced into Congress in early 1935, by Senator Wagner and Representatives Doughton and Lewis, which resulted in the Social Security Act, approved by the President August 14, 1935.

Two titles of the Social Security Act—titles IX (which later became section 1600 of the Internal Revenue Code) and III—related to unemployment compensation. The former provides for an excise tax of 3 per cent on the pay rolls of all employers who have in any year as many as eight employees for 20 weeks in industrial

and commercial employments, excluding chiefly the agricultural, domestic, and governmental service, and that for nonprofit institutions. Against this tax the employer can credit payments made, or credits secured by him, under an approved State unemployment compensation law, but the credit cannot exceed 90 per cent of the Federal tax, or 2.7 per cent. In addition to credits allowed for payments actually paid under a State law, the employer can also secure credit for payments forgiven through the assignment to him by the State of a rate less than 2.7 per cent when the reduced rate is allowed, in accordance with Federal standards, on the basis of his experience, during not less than 3 years, with unemployment or other factors directly related to unemployment risk. In order to be approved for such tax-credit purposes, the State law must provide that all benefits be paid through public employment offices or such other agencies as the Federal Security Administrator may approve; that all payments collected under the State law must be immediately deposited in an Unemployment Trust Fund in the United States Treasury in which it is kept to the account of the State; that any money withdrawn by the State from the Unemployment Trust Fund must be used exclusively for the payment of unemployment compensation; that benefits may not be denied to any person for refusing to accept new work if the position is vacant because of a labor dispute, if the wages, hours, or conditions of the work are substantially less favorable to the individual than those prevailing for similar work in the locality or if as a condition of being employed the worker would have to resign from or refrain from joining a labor organization or would be required to join a company union.

Title III of the Social Security Act provides for grants to the States for the total cost of proper and efficient administration of their unemployment insurance laws. In order to be eligible for such grants, the State law must meet the conditions outlined above and in addition must provide such methods of administration as are reasonably calculated to insure the full payment of benefits when due, opportunity for a fair hearing before an impartial tribunal for all whose claims to benefit are denied, and provision of full and complete reports, as required by the Federal Security Administrator, on the activities under the State law, and of information as requested by other Federal agencies engaged in the administration of public works or assistance through public employment.

In addition, title IV of the War Mobilization and Reconversion Act of 1944 provides for making loans to a State when its unemployment fund begins to run low.

It is apparent that the provisions of the Federal law do not in themselves provide for the payment of unemployment insurance benefits. Rather, a Federal-State system was established under

which strong incentives were provided by the Congress, through the tax credit allowed employers and the grant for the costs of State administration, for the States to enact laws providing for the payment of benefits. The character of the unemployment tax has determined in large part the scope and coverage of the State unemployment insurance laws and the financial structure but there is nothing in the Federal acts which limits a State in the number or classes of workers, occupations or industries it should cover, in the qualifying requirements, in terms of previous wages or employment it may require as a condition of benefits, the benefit amount it may pay, the period for which benefits may be paid, or the disqualifications that may be imposed save, as noted above, that certain safeguards are required to be maintained to prevent an undermining of labor standards.

While the passage of the Social Security Act did not result immediately in the Nation-wide enactment of unemployment compensation laws, largely because of early doubts as to the constitutionality of the act, in less than 2 years after the act was passed, unemployment compensation laws existed in every State, two territories, and the District of Columbia, and by January 1939 unemployment compensation benefits were payable in all these jurisdictions.

State legislatures, in imposing taxes for unemployment insurance, have been strongly influenced by the application of the Federal Unemployment Tax. This is especially true regarding the exemptions from the application of the tax of certain types of employment, for instance, domestic service, agricultural labor, and service for nonprofit organizations. However, in one respect the States have gone considerably beyond the limitations of the Federal tax; whereas it applies only to employers having eight or more individuals in their employ, only 22 States are so limited. Indeed, 17 States require unemployment insurance taxes from employers having only one employee. Although there has been some expansion of coverage into certain segments of the agricultural and domestic service labor force, it appears clear that no broad expansion of coverage in these areas will occur until the Federal Unemployment Tax applies to such areas.

The Unemployment Tax Act has also had a strong influence on the financial structure of the program. While nine States have at one time or another required contributions to the Unemployment Fund from employees as well as employers, only two now do so. Originally, the States were required to collect contributions for 2 years prior to paying benefits. Since the tax rate was 1 per cent in 1936 and 2 per cent in 1937, States generally had an initial reserve of 1 year's contributions at the standard rate of 2.7 per cent when they began paying benefits. However, all States have now taken

advantage of the right to permit reduced rates to employers on the basis of their experience with unemployment. There is great variation in the extent to which the rates have been reduced under State laws—in 1948 the average tax was as low as .3 per cent in one State and as high as 2.1 per cent in another—the total effect has been to lower tax rates to 1.2 per cent for all States as a whole. In accordance with the Federal act, none of these reductions have been made uniformly, State-wide, but only to an individual employer on the basis of his experience. Nevertheless, there is great variation among the States in the methods and formulas used to measure an employer's experience and to translate that experience into a rate of taxes or contributions.

States have used the freedom granted by the Federal act to vary considerably in the extent of benefit protection afforded those in employment subject to their laws, although most States use a report of the individual worker's wages, as reported quarterly by his employer, as the basis for determining his qualification for benefits, his weekly benefit amount, and the duration of benefits. The "base period," used for determining attachment to the labor market and hence qualification or eligibility for benefits, may be uniform for all claimants or individual, i.e., determined in relation to the beginning of the individual's unemployment. Similarly, the "benefit year," within which his weekly benefit amount is unchanged and within which his benefits are limited, may be uniform or individual. He may qualify for benefits if he earned 18 times his weekly benefit amount in one State, while another may require 40 times. Other States may require a flat amount of earnings, ranging from \$100 to \$600, or a number of weeks of employment. The waiting-period before any week for which benefits are payable varies from none at all to 2 weeks of total unemployment. The weekly benefit amount is determined in varying ways, although usually in some fraction of the wages in the highest quarter of the base period. The maximum weekly benefit is commonly \$20 but may be as high as \$26 or as low as \$15. Additional allowances for dependents are given in eleven States, in varying amounts and with varying definitions of dependents. Duration of benefits may be the same for all eligible claimants or may vary in relation to past earnings and the maximum duration may be as little as 12 weeks or as much as 26 weeks. The reasons for disqualification are chiefly four: voluntary leaving of work, discharge for misconduct, refusal of suitable work, and unemployment due to a labor dispute. However, there may be many more, such as those for leaving due to marital or domestic responsibilities or pregnancy, and the disqualification may be of varying severity, from a few weeks' postponement of benefits to the cancellation of all rights to benefits.

In the 14 years of its history, the unemployment compensation program in this country has progressed rapidly in providing security to the unemployed. Through the end of 1948, \$5.3 billion had been paid in benefits and a reserve fund of \$7.6 billion accumulated. Benefit rights have been extended in regard to weekly benefit amounts and duration, though restricted in other respects. As with all dynamic programs with great social import, the unemployment compensation program is faced with important problems. Among them is the fundamental one of the proper place of unemployment compensation in the total of all governmental and private endeavors to provide security to the employed and unemployed; this involves questions as to the proper coverage of the labor force, and the adequacy of the weekly amount and of the potential duration of benefits, in view of the ultimate need for such provision for the unemployed as will assure a healthy economy, high national productivity, and a continually efficient labor force. Another problem is that created by conflicts between the employer and the employee which often lose sight of the objectives of the program. These conflicts arise partly out of the existing plan of financing the program through contributions or taxes paid by employers, subject to reduction on the basis of his "experience." A third problem is that arising out of the State-by-State character of the benefit provisions of the program and requires a careful judgment of the relative weights of the advantages and disadvantages of State experimentation and self-determination in areas where the national welfare is so much at stake.