

## Part IV

# UNEMPLOYMENT INSURANCE

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### INTRODUCTION AND SUMMARY

#### *Characteristics of State-Federal Unemployment Insurance*

During the long and deep depression of the 1930's, the United States became acutely aware of the plight of millions of men and women who were unemployed through no fault of their own. Although up to that time, only one State had enacted an unemployment insurance law, the Federal Government took steps in 1935 to provide unemployment insurance at an early date for a large proportion of the industrial and commercial labor force. The Social Security Act of 1935, however, did not set up a single Federal system of unemployment insurance. Rather, through a tax-offset device, it encouraged the States to establish their own systems conforming to a few broad Federal standards. Within 2 years, the 48 States, the District of Columbia, Alaska, and Hawaii had unemployment insurance laws.

The Federal Government levies a 3 percent tax on the pay rolls of employers in business and industry who have eight or more employees. This tax can be offset—up to 90 percent—by contributions paid by employers under approved State laws. A State law can be approved only if the funds collected under it are deposited to the State's account in a trust fund in the Federal Treasury to be used by the State exclusively for the payment of unemployment insurance benefits. Furthermore, the benefits provided under the State law must be paid through public employment offices "or such other agencies as the Federal Security Administrator may approve." In general, no Federal standards have been established relating to such benefit rights as the amount or duration of benefits. One Federal standard relating to benefits, however, was set as a condition for tax offset; namely, that benefits under the State law shall not be denied to any otherwise eligible individual for refusing to accept new work (1) if the position offered is vacant due directly to a labor dispute; (2) if the working conditions offered are substantially less favorable than those prevailing for similar work in the locality; or (3) if, as a condition of employment, the individual must join a company union or resign from or refrain from joining any bona fide labor organization.

As an incentive to employment stabilization, employers were allowed credit against the Federal tax, not only for contributions actually paid, but also for contributions which were waived because the employer's contribution rate was reduced by the State on the basis of his experience with unemployment "or other factors directly related to unemployment risk."

In addition to stimulating the enactment of State unemployment insurance laws, the Federal Government undertook to assure adequate

Nation-wide provision for administering the program, by authorizing grants to States to meet the total cost necessary for proper and efficient administration of their laws. Although technically made from the general Federal Treasury, it is clear from the hearings and committee reports that these grants were thought of as being financed by the 0.3 percent of covered pay rolls which constitutes the income to the Federal Government from the Federal Unemployment Tax Act. These administrative grants were to enable, and also require, the States to use methods of administration reasonably calculated to insure the full payment of benefits when due, to provide for fair hearings to those whose claims are denied, to make reports, and to cooperate effectively with public works agencies and the Railroad Retirement Board. A State was not entitled to the grants if these conditions were not met or if, in the administration of the State law, benefits were denied in a substantial number of cases to individuals entitled thereto under the State law. Except for these very general Federal standards, each of the 51 systems has established its own eligibility requirements, benefit amounts and duration, waiting periods, disqualification rules, and administrative procedures.

The Council has studied the present State-Federal arrangements, and the majority approves the basic principles of the system. In the opinion of the majority (1) the State is the proper unit to determine the benefit provisions which will meet the varying conditions in different parts of the country; (2) State laws can assure more adequate benefits in highly industrialized areas; and (3) the State-Federal program has shown over the past 10 years that it is capable of making progress. In most States the minimums, maximums, and average weekly payments have risen, durations have increased, waiting periods have decreased, and coverage has broadened.

Five members of the Council, however, favor the establishment of a single national system of unemployment insurance. (See appendix IV-C.) In their opinion unemployment is essentially a national problem and is an inappropriate area for State operation. They point out that many workers move from State to State in their search for work and that labor markets cut across State lines. The maintenance of 51 separate systems, each with its own reserve, is in their opinion actuarially unsound. They also feel that the effectiveness of the various State plans has been diminished by the growing restrictions on benefits and that the progressive changes in the benefit provisions of State laws have not kept pace with increasing wages and prices. Four of these members would join with the majority, however, in the recommendations included in this report for the improvement of the State-Federal system should the Congress decide against the establishment of a national program. One member is not signing the recommendations of the Council since he disagrees with some of the most important ones even under a continued State-Federal system. (See appendix IV-C.)

### ***Deficiencies in the Present Program***

The dual nature of the State-Federal plan for unemployment insurance has limited the scope of the Council's work. Since the actual administration of unemployment benefits is the responsibility of 48 States, the District of Columbia, and the Territories of Alaska and

Hawaii, it would have been impracticable for the Council to have made a detailed investigation of administration in each jurisdiction. The Council, however, has studied the basic principles and operations of the State-Federal program and finds five major deficiencies:

1. *Inadequate coverage.*—Only about 7 out of 10 employees are now covered by unemployment insurance.

2. *Benefit financing which operates as a barrier to liberalizing benefit provisions.*—The present arrangements permit States to compete in establishing low contribution rates for employers and therefore discourages the adoption of more adequate benefit provisions.

3. *Irrational relationship between the contribution rates and the cyclical movements of business.*—The present arrangements tend to make the contribution rate fluctuate inversely with the volume of employment, declining when employment is high and when contributions to the unemployment compensation fund are easiest to make and increasing when employment declines and when the burden of contributions is greatest.

4. *Administrative deficiencies.*—Improvement is needed in methods of financing administrative costs, provisions for determining eligibility and benefit amount in interstate claims, procedures for developing interstate claims, and methods designed to insure prompt payments on all valid claims and to prevent payments on invalid claims.

5. *Lack of adequate employee and citizen participation in the program.*—Workers now have less influence on guiding the administration of the program and developing legislative policy than they should, and some employees, employers, and members of the general public tend to regard unemployment compensation more as a hand-out than as social insurance earned by employment, financed by contributions, and payable only to those who satisfy eligibility requirements.

The Council has also made recommendations on other points, but has mainly proposed measures designed to remedy these major defects. The recommendations apply only to the continental United States, Hawaii, and Alaska. The Council, in its report on old-age and survivors insurance, proposed that a special commission should be established to determine the various types of social-security protection appropriate to Puerto Rico, the Virgin Islands, Guam, and other possessions of the United States.<sup>1</sup>

### ***Recommendations for Improvement of the Program***

A summary of the Council's recommendations follows:

1. *Employees of small firms.*—The size-of-firm limitation on coverage in the Federal Unemployment Tax Act should be removed, and employees of small firms should be protected under unemployment insurance just as they are now protected under old-age and survivors insurance.

2. *Employees of nonprofit organizations.*—The Federal Unemployment Tax Act should be broadened to include employment by all nonprofit organizations, except that services performed by clergymen and members of religious orders should remain excluded. The exclusion of domestic workers in college clubs, fraternities, and sororities by the 1939 amendments to the Federal Unemployment Tax Act

<sup>1</sup> See p. 28.

should be repealed so that these workers will again be protected under all State laws.

3. *Federal civilian employees.*—Employees of the Federal Government and its instrumentalities should receive unemployment benefits through the State unemployment insurance agencies in accordance with the provisions of the State unemployment insurance laws. The States should be reimbursed for the amounts actually paid in benefits based on Federal employment. If there is employment under both the State system and for the Federal Government during the base period, the wage credits should be combined and the States should be reimbursed in the proportion which the amount of Federal employment or wages in the base period bears to the total employment or wages in the base period. The special provisions for federally employed maritime workers should be extended until this recommendation for covering all Federal employees becomes effective.

4. *Members of the armed forces.*—Members of the armed forces who do not come under the servicemen's readjustment allowance program should be protected by unemployment insurance.

5. *Borderline agricultural workers.*—To afford protection to certain workers excluded by the 1939 amendments to the Federal Unemployment Tax Act, defining agricultural labor, coverage of that act should be extended to services rendered in handling, packing, packaging, and other forms of processing agricultural and horticultural products, unless such services are performed for the owner or tenant of the farm on which the products are raised and he does not employ five or more persons in such activities in each of four calendar weeks during the year. Coverage should also be extended to services now defined as agricultural labor by section 1607 (1) (3) of the Unemployment Tax Act.

6. *Inclusion of tips in the definition of wages.*—The definition of wages contained in section 1607 (b) of the Federal Unemployment Tax Act should be amended to specify that such wages shall include all tips or gratuities customarily received by an employee from a customer of an employer.

7. *Contributory principle.*—To extend to unemployment insurance the contributory principle now recognized in old-age and survivors insurance, a Federal unemployment tax should be paid by employees as well as employers. Employee contributions to a State unemployment-insurance fund should be allowed to offset the Federal employee tax in the same manner as employer contributions are allowed to offset the Federal tax on employers. The employee tax would be collected by employers and paid by them when they pay their own unemployment tax.

8. *Maximum wage base.*—To take account of increased wage levels and costs of living, and to provide the same wage base for contributions and benefits as that recommended for old-age and survivors insurance, the upper limit on earnings subject to the Federal unemployment tax should be raised from \$3,000 to \$4,200.

9. *Minimum contribution rate.*—The Federal unemployment tax should be 0.75 percent of covered wages payable by employers and 0.75 percent payable by employees. The taxpayer should be allowed

to credit against the Federal tax the amount of contributions paid into a State unemployment fund, but this credit should not exceed 80 percent of the Federal tax. Since no additional credit against the Federal tax should be allowed for experience rating, the States would, in effect, be required to establish a minimum rate of 0.6 percent on employers and 0.6 percent on employees.

10. *Loan fund.*—The Federal Government should provide loans to a State for the payment of unemployment-insurance benefits when a State is in danger of exhausting its reserves and covered unemployment in the State is heavy. The loan should be for a 5-year period and should carry interest at the average yield of all interest-bearing obligations of the Federal Government.

11. *Standards on experience rating.*—If a State has an experience rating plan, the Federal act should require that the plan provide: (1) a minimum employer contribution rate of 0.6 percent; (2) an employee rate no higher than the lowest rate payable by an employer in the State; and (3) a rate for newly covered and newly formed firms for the first 3 years under the program which does not exceed the average rate for all employers in the State.

12. *Combining wage credits earned in more than one State and processing interstate claims.*—The Social Security Administration should be empowered to establish standard procedures for combining unemployment-insurance wage credits earned in more than one State and for processing interstate claims. These procedures should be worked out in consultation with the administrators of the State programs and should provide for the combination of wage credits not only when eligibility is affected but also when such combination would substantially affect benefit amount or duration. All States should be required to follow the prescribed procedures as a condition of receiving administrative grants. Similar procedures should be worked out, in cooperation with the Railroad Retirement Board, for combining wage credits earned under the State systems and under the railroad system.

13. *Financing administrative costs.*—Income from the Federal Unemployment Tax Act should be dedicated to unemployment-insurance purposes. One-half of any surplus over expenses incurred in the collection of the tax and the administration of unemployment insurance and the employment service should be appropriated to the Federal loan fund, and one-half of the surplus should be proportionately assigned to the States for administration or benefit purposes. A contingency item should be added to the regular congressional appropriation for the administration of the employment-security programs. The administrative standards in the Social Security Act should be applicable to the expenditure of the surplus funds as well as to expenditures of the funds originally appropriated.

14. *Clarification of Federal interest in the proper payment of claims.*—The Social Security Act should be amended to clarify the interest of the Federal Government not only in the full payment of benefits when due, but also in the prevention of improper payments.

15. *Standards for disqualifications.*—A Federal standard on disqualifications should be adopted prohibiting the States from (1) re-

ducing or canceling benefit rights as the result of disqualification except for fraud or misrepresentation, (2) disqualifying those who are discharged because of inability to do the work, and (3) postponing benefits for more than 6 weeks as the result of a disqualification except for fraud or misrepresentation.

16. *Study of supplementary plans.*—The Congress should direct the Federal Security Agency to study in detail the comparative merits in times of severe unemployment of (a) unemployment assistance, (b) extended unemployment-insurance benefits, (c) work relief, (d) other income-maintenance devices for the unemployed, including public works. This study should be conducted in consultation with the Social Security Administration's Advisory Council on Employment Security, the Council of Economic Advisers, and the State employment security agencies, and should make specific proposals for Federal measures to provide economic security for workers who do not have private or public employment during a depression and who are not adequately protected by unemployment insurance.

### ***Plan of the Report***

The Council's proposed remedies for the five major deficiencies of the present program are summarized in this section, which also includes a discussion of the need for a broad informational program. The section which follows presents the 16 specific recommendations in more detail. The report proper concludes with a discussion of temporary-disability insurance. The appendixes include cost estimates for unemployment insurance, material on the proper payment of benefits, dissents, and statistical information on the operation of the programs.

### ***Goal of Universal Coverage***

At present about 7 out of 10 jobs in American industry are covered by unemployment-insurance laws. It would obviously be desirable, if practicable, to have all jobs covered. In unemployment insurance, however, universal coverage would entail more difficult administrative problems than would be met in old-age and survivors insurance. The Council, therefore, does not recommend that the Federal Unemployment Tax Act be extended now to include the two groups which would present the greatest administrative difficulty—farm workers and domestic workers—and, in view of constitutional limitations, the coverage of employees of State and local governments will have to be left to the States.<sup>2</sup>

The Council favors the immediate extension of the Federal Unemployment Tax Act to the areas of employment that present no overwhelming administrative or legal difficulties—namely, to employment by small firms, by nonprofit organizations, by the Federal Government (both civil and military), and to certain borderline agricultural employments. Such extension might increase coverage in an average week by over 7 million or to about 85 percent of the total number of individuals employed by others.

<sup>2</sup> Extension of compulsory coverage to workers engaged in the "proprietary" functions of government—as opposed to regular governmental functions—is, in all probability, constitutional. In a State-Federal program, however, the Council believes that it would be better for States to provide for covering all governmental employees under one plan rather than, in effect, to force the coverage through Federal law of those governmental workers engaged in "proprietary" activities.

In absolute terms, the number of individuals in employment covered by the State unemployment-insurance laws has increased markedly in the past 10 years. This increase is shown in the following table:

TABLE A.—Average monthly covered employment, 1938-48

[In millions]

	<i>Covered workers</i>		<i>Covered workers</i>
1938.....	19.9	1944.....	30.0
1939.....	21.4	1945.....	28.4
1940.....	23.1	1946.....	30.2
1941.....	26.8	1947.....	32.2
1942.....	29.3	1948 (June).....	32.6
1943.....	30.8		

Much of this increase has resulted from the increase in the active labor force of the United States. In considerable measure, however, the increase also reflects changes in the size of firm covered by State laws. The original laws of 33 States limited coverage to commercial and industrial workers in firms with 8 or more employees in at least 20 weeks in a calendar year. In 1948, 17 States covered employees in firms with 1 or more persons, although only 6 of the laws applied without restriction as to the number of workers, length of employment, or size of pay roll; and only 22 States still excluded from coverage employees of firms with less than 8 persons (table 2, appendix IV-E). The laws of 29 States contain provisions which will automatically extend coverage to smaller firms to the extent that the Federal size-of-firm restriction is reduced.

While progress has been made in extending coverage to smaller firms, maritime services represent the only type of work originally excluded to which coverage has been extended on a general scale. Effective July 1, 1946, Congress extended the Federal unemployment tax to services in private maritime employment and the States with maritime firms amended their laws accordingly. As early as 1944, a few States had already extended coverage to maritime workers following a Supreme Court decision that the Constitution did not prohibit such coverage under State laws. In addition, the War Mobilization and Reconversion Act of 1944 provided reversion benefits for federally employed seamen.

The Federal Unemployment Tax Act now excludes agricultural labor; domestic service in a private home; service of an individual for his son, daughter, or spouse, or of a minor child for a parent; services for Federal, State, or local governments, or for foreign governments; services for nonprofit, religious, charitable, educational, scientific, or humane organizations; casual labor not in the course of the employer's business; and miscellaneous services such as services as a student nurse or interne, service for employees' beneficial associations, domestic service for college clubs, and services for organizations exempt from Federal income tax if the remuneration is not more than \$45 in a calendar quarter. Railroad employment, which was originally covered, is now under a separate Federal unemployment insurance system.

The occupational exclusions in State laws are in most cases the same as those in the Federal act, but several States have provided for broader coverage. New York from the outset has covered domestic workers in a home with four or more domestics, and in 1947 New York provided protection for State employees. Wisconsin has covered some State and local government employees from the beginning. Hawaii in 1945 and Tennessee in 1947 extended coverage to nonprofit organizations, excluding ministers, members of religious orders, and, in Tennessee, executives and members of the teaching staffs of educational institutions. A few additional States cover some employment by nonprofit organizations. Many States have contemplated coverage extension and would automatically cover additional occupations if and when the Federal act is extended.

In an average week during the year ended June 30, 1948, the total labor force contained 62 million persons, of whom 2.1 million were unemployed and 59.9 million were employed. The employed labor force comprised 12.8 million self-employed persons and unpaid family workers and 47.1 million employees. About 70 percent of the employees, or 32.9 million of the 47.1 million, were covered by some unemployment insurance program. About 14.2 million employees, or 30 percent of those employed by others, were in employments which carried no form of unemployment insurance protection. The following table shows the distribution of the total labor force by coverage status:<sup>3</sup>

TABLE B.—Total labor force by coverage status in an average week of year ended June 30, 1948

	<i>Persons in millions</i>
Total labor force.....	62.0
Unemployed.....	2.1
Employed, total.....	59.9
Self-employed and unpaid family workers.....	12.8
Farm operators and unpaid family workers.....	6.3
Urban self-employed and unpaid family workers.....	6.5
Employed by others.....	47.1
Covered by unemployment insurance.....	32.9
State laws.....	31.3
Federal program for railroad workers.....	1.6
Not covered by unemployment insurance.....	14.2
Small firms.....	3.4
Employees of nonprofit organizations.....	.9
Federal employees.....	1.7
Armed forces.....	1.3
Agricultural workers.....	1.7
Domestic workers in private homes.....	1.7
Employees of State and local governments.....	3.5

<sup>3</sup> Data on labor force, unemployed and total employed, from Monthly Report on the Labor Force, Bureau of the Census; employment covered by unemployment insurance, estimated by the Bureau of Employment Security; employment not covered by unemployment insurance, from Bureau of the Census, adjusted by Bureaus of Old-Age and Survivors Insurance and Employment Security.

Some involuntarily unemployed persons will probably continue to be outside the scope of unemployment insurance even if "universal coverage" is achieved. Those seeking jobs for the first time or after a long absence from the labor market form one such group. Another is made up of those who are intermittently in and out of the labor market, but never in for very extended periods. Persons formerly dependent on self-employment but now, for one reason or another, seeking work as employees are a third group. It is probably not feasible to cover the self-employed against the risk of losing their self-employment, for it would be extremely difficult to determine when a self-employed person becomes unemployed. If his business declined gradually, it would be almost impossible to determine at what point he actually became available for employment by another. A further difficult problem would be to determine whether his unemployment was involuntary or merely the result of his decision to give up his business.

The Council's goal for coverage in unemployment insurance is the protection of all persons who work for others and have a recent record of depending on wages for a significant part of their support. This goal must be obtained gradually. The Council believes that the Federal Government cannot reasonably require the States to cover all workers immediately. The Council hopes, however, that some of the States will take advantage of the opportunity to assume leadership in extending coverage to domestic workers in private homes and to a larger part of farm employment than we believe should be covered immediately under the Federal act. The State-Federal program permits States wishing to make progressive changes in the program to take such steps before other States are willing to do so.

If the old-age and survivors insurance system is extended to virtually all who work, as recommended by the Council in its first report,<sup>4</sup> the resulting experience should be available for solution of the reporting problems connected with the extension of unemployment insurance to agricultural and domestic workers. The Council believes that this experience should be made available to the States and that the wage reports obtained under old-age and survivors insurance should be offered to the States on a cost basis.

### ***Benefit Financing Designed To Encourage the Adoption of Adequate Benefit Provisions***

The Council believes that liberalization of the benefit, duration, and eligibility conditions in the State laws is generally needed. Unemployment-insurance payments should be as high a proportion of wage loss caused by unemployment as is practicable without inducing people to prefer idleness to work. The higher the ratio of unemployment benefits to wage loss caused by unemployment, the more effectively unemployment insurance limits the tendency for the reduced purchasing power of unemployed persons to create more unemployment. Liberalization of unemployment compensation should take the form of (1) more liberal eligibility requirements; (2) higher benefits in relation to wages; and (3) longer duration of benefit payments.

<sup>4</sup> See p. 6.

Considerable progress has been made in the last 12 years in liberalizing benefit provisions in the State laws. Today, for example, 40 States pay benefits for 20 weeks or more (table 7, appendix IV-E), while in 1937 there were only 5 States which provided for duration of 20 weeks or more; in 1948 there are 41 States which pay a maximum weekly benefit of \$20 or more (table 5, appendix IV-E), while in 1937 there were no such States. To some extent these gains have been limited by stricter eligibility requirements and despite the progress made in liberalizing unemployment insurance programs, it is estimated that approximately 27 percent of the beneficiaries in 1948 exhausted their benefit rights while still unemployed. Benefit amounts are generally still too low in relation to wages. Satisfactory estimates of the fraction of wage loss caused by the unemployment of covered workers that is compensated by unemployment benefits are not available, but rough calculations indicate that it is probably not more than 25 percent. As a result, unemployment compensation as it is today would have a very limited value in checking the cumulative increase of unemployment.

One way of encouraging liberalization of unemployment compensation would be to impose Federal standards for eligibility, duration, and benefit amount. The Council has carefully considered such standards and has decided not to recommend them. Such an approach seems to the majority of the Council to be unduly complicated as well as inappropriate in a State-Federal system. The Council believes that the best way to encourage the liberalization of unemployment compensation is to remove, or at least greatly diminish, the incentive which States now have to reduce their unemployment insurance contribution rates.

The Federal Unemployment Tax Act was passed, in part, to equalize the tax burden on employers regardless of the State in which they did business. Before the Federal tax was imposed, State legislatures were reluctant to establish unemployment compensation systems because of the fear of placing local employers at a disadvantage in competing with employers in States which did not require unemployment contributions.

The objective of eliminating interstate competition has been only partially realized and a strong incentive to reduction of contribution rates remains. Since the Federal tax rate of 3 percent may be offset up to 90 percent not only by actual payments to a State unemployment insurance system, but also by credits for experience rating, the tax burden on employers is allowed to vary considerably from State to State (table 10, appendix IV-E).

All States now have some form of experience rating. This fact, however, does not necessarily reflect their belief in the efficacy of experience rating as a device for inducing employers to regularize employment. Under the Federal act, experience rating is the only way that State contribution rates can be reduced below 2.7 percent (90 percent of 3 percent), and since in all likelihood no State would need such a high rate even for a greatly liberalized benefit system, the States have adopted experience rating as a rate-reduction device.

Unfortunately, the present law places no floor under rate reduction through experience rating. The contribution rate may be set at zero for a large group of employers, and the average for the whole State

may drop to very low levels. In the year 1948, 15 States had average rates of 1 percent or less (table 10, appendix IV-E). While the Federal law set rates higher than now seem necessary, many States have gone to the other extreme and are collecting contributions which in all probability are considerably below the average rate necessary to finance an adequate system of benefits over the next 10 years, even if their existing reserves in the unemployment trust fund are utilized extensively. Now, in a period of full employment, rates should certainly be at least as high as the average rate which will be needed over the next 10 years. Employers can now afford to pay higher rates and, on general economic grounds, rates should not be stepped up when unemployment is on the increase.

The Council is concerned that, under present arrangements, contribution rates will tend to become inadequate in more and more States. Employers are, of course, interested in rate reductions, and, since they pay the full cost of the present system, their wishes have considerable weight with legislatures and the public. Under present conditions, any proposal for more liberal benefits must be weighed against the cost to the employer and his tax position in relation to employers in other States.

The Council proposes two remedies for this situation: (1) The equal sharing of costs by employer and employee, and (2) the imposition of a Federal minimum for the State contribution rate, so that the rate will not be allowed to fall below a point which will be sufficient to pay adequate benefits in the great majority of States.

The Council believes that the proposed minimum rate, greatly reducing interstate competition for rate reduction and providing adequate funds for the majority of State systems, would result in considerable liberalization of benefit provisions.

Under such a plan there would no longer be strong inducements for a State to keep benefits below a reasonable amount. Low benefits would not hold out the possibility of lower contributions as they do now, but would merely result in an accumulation of ever-larger reserves.

### ***Developing a More Rational Relationship Between Contribution Rates and Cyclical Movements of Business***

A minimum contribution rate would also go far toward promoting a more rational relationship between the rate of contribution and the cyclical movements of business. In most States, experience rating, at least as practiced thus far, means that a favorable period of employment reduces the ratio of the employer's contributions to his pay rolls, while an unfavorable period of employment increases this ratio. Some types of experience rating create a closer relationship than others between recent changes in the volume of employment and the contribution rate, but all types—in greater or lesser degree—tend to vary the contribution rate inversely with the volume of employment.

The tendency for the rate of unemployment contributions to rise as employment decreases can have serious consequences for the economy. For example, today when employment is high and the demand for goods urgent, many employers are paying contributions at a lower rate than they can expect to pay, on an average, over a period of years. If business and employment were to decline and if unemployment were to rise, these employers would have to contribute at

higher rates, at the very time when prices were falling, when business profits were diminishing, and when business concerns were having increasing difficulty in meeting their obligations.

Under the Council's proposal for a minimum contribution rate, this tendency would be substantially reduced in States which retain experience rating. The minimum rate would reduce the possible range by requiring States to charge more than they might otherwise charge in periods of full employment, thus reducing their need to raise rates in periods of increasing unemployment. In the majority of States, the minimum rates will be sufficient for an adequate system of benefits and presumably would be the rate charged all employers and employees at all times.

The Council believes that it would be quite unfortunate if a rise in unemployment were to result in increasing the contribution rate when markets are falling. The Council has therefore proposed, in addition, a Federal loan fund, so that, if necessary, a State may borrow rather than increase the contribution rates while unemployment is rising. The Federal loan fund would make it possible for States to pay more liberal benefits with a given contribution rate, but neither the loan fund nor the Federal minimum rate would relieve a State from considering solvency problems in the light of its own contribution rate, reserve funds, and unemployment experience.

### *Setting the Minimum Contribution Rate*

The Council has proposed a Federal tax rate of 0.75 percent of covered wages payable by employers and 0.75 percent payable by employees, with a credit up to 80 percent for contributions paid into a State unemployment fund. This proposal would result in a minimum State contribution at the combined rate of 1.2 percent.

Appendix IV-A discusses in detail the method of arriving at this minimum rate. In general, it was necessary to assume certain illustrative benefit plans as "adequate" and then to estimate the cost of such plans in the various States. These costs were estimated under two widely differing hypothetical sets of economic conditions for the next 10 years, and the actual cost was assumed to fall within the resulting range.

The Council emphasizes the difficulties of estimating the costs of unemployment insurance. No one can predict with assurance the pattern of employment and unemployment over even as brief a period as the next 10 years. Unemployment insurance has certain self-limiting factors, however, which reduce the effect of large-scale unemployment on costs. The program, in the first place, is not designed to compensate for long-term unemployment, and the eligibility requirements also serve to reduce the liability of the system during a depression. We believe, therefore, in spite of the uncertainty of the economic assumptions, that our estimates provide a sufficient basis for establishing minimum rates on a national basis.

A minimum rate which will adequately finance a given level of benefits in some States is bound to be too low in others, while some States will be able to finance more liberal benefits at the same rate. In selecting a minimum rate to recommend, therefore, the Council had to decide whether to recommend (1) a rate that would be high enough to finance an "adequate" system of benefits in all States but would be higher than necessary in most, (2) a rate that would be just

sufficient to supply an adequate level of benefits in the States with the lowest costs but would be too low for most States, or (3) a rate that falls between these two extremes and is about right for the majority of States.

The Council has decided in favor of the third of these approaches; it is therefore necessary to emphasize that the rate should be thought of strictly as a minimum rate and that several States will need to charge higher rates to support an adequate system of benefits. According to our estimates based on past benefit experience, the minimum rate of 1.2 percent would be applicable to at least 30 States within a relatively narrow range of adjustment in benefits or contributions under all of the economic and benefit assumptions used. Contributions in 5 States would undoubtedly have to be higher to support a benefit structure that could be considered adequate, and the past benefit experience of 3 others indicates costs so low that reserves would increase under even more pessimistic assumptions than 2 to 10 million unemployed. The 1.2 percent rate is reasonably applicable to various States among the remaining 13 depending on which set of assumptions is used and how large a reserve is assumed to be desirable at the end of the 10-year cycle.

In recommending a combined minimum contribution rate of 1.2 percent, the Council has assumed that in meeting benefit costs most States during the next 10 years will utilize a portion of their currently large reserves as well as contributions.

### ***Promoting Greater Employee and Citizen Participation***

The Council is impressed by evidence that, in general, the workers covered by unemployment-insurance laws lack an adequate sense of participating in the programs. Their failure to concern themselves with unemployment insurance may in part be the cause of the unduly strict eligibility requirements and disqualification provisions in some States. The Council finds several reasons for this lack of a sense of participation. One is probably the fact that the volume of unemployment during the last few years has been very small and jobs have usually been easy to obtain. Another is the fact that since the payroll contribution is paid solely by the employer, the employee does not have the sense of making a direct contribution each week to his protection against unemployment.

The Council believes that it is vitally important to have both employees and managements take a lively interest in the system of unemployment compensation and feel keenly concerned about providing the best possible administration and adequate benefits. Only keen interest on the part of the covered employees and managements will keep the unemployment compensation system adjusted to changing conditions and will assure the best possible administration. To this end, the Council proposes that employees contribute as they do for old-age and survivors insurance.

The Council also recommends that advisory councils composed of representatives of management, employees, and the general public be established and encouraged to assume an active role in advising on the formulation of legislative and administrative policy. The Council believes that these three groups must be kept fully informed and abreast of current developments and that advisory councils provide one way of accomplishing that purpose.

A Federal Advisory Council on Employment Security has recently been established. Forty-five States provide for State-wide councils with equal representation of labor and management groups and all but one provide for one or more public members. In 41 States these councils are mandatory and in 4 permissive; in over half of these States, the administrative agency appoints the councils; in less than half, the governor; and in 3, the governor on the recommendation of the State agency. In several States, such as New York, Connecticut, Massachusetts, Illinois, Wisconsin, and Utah, the councils have met frequently and played an important role, but in some others they are inactive. State advisory councils on employment security should be encouraged to assume an active role in the program.

### ***Promoting Improved Administration***

Efficient and equitable administration is of the utmost importance in unemployment insurance, since a large number of administrative decisions must be made continually and rapidly to determine if a person is eligible for benefits. The need for high quality in administration is most apparent in those aspects of the program which involve the determination of current eligibility for benefits and direct contact with claimants. In these aspects of the program, efficient procedures for claims taking, interviewing, and reconsidering claims and appeals are essential to adequate fact finding and correct determination of rights to benefits, a determination that assures both full and prompt payment of benefits to claimants entitled to them and denial of benefits to those who are not eligible.

The Council recognizes that responsibility for the fair and efficient administration of the unemployment-insurance programs is primarily the responsibility of each State. The quality of administration will necessarily depend in large part on the caliber of the personnel selected to do the State job. There can be no substitute for a career service with high standards of job performance and careful training for the complicated task of administering unemployment insurance. The Federal Government, however, has an important role in administration in enforcing minimum standards and in providing administrative funds.

There is considerable evidence to indicate that the funds supplied for administration in the past have not been sufficient to support the most efficient kind of administration. The Council believes further that the present arrangements for financing the administration of unemployment insurance are unduly rigid and do not give the State agencies sufficient opportunity to experiment in improving administration. The Council, therefore, recommends changes in the methods of financing administration which will provide additional funds for State administration of unemployment insurance. These funds would enable some States to pioneer in administration and do more than the minimum which the Federal Government is willing to approve as necessary for all States. The purpose can be accomplished by providing that some funds which could be used for administration be automatically assigned to the States. Because of great variation in work loads depending on the level of unemployment, a large contingency fund should be authorized in addition to the regular appropriations to the States and the Social Security Administration.

Although the Federal law provides specific authority for requiring "such methods of administration as are reasonably calculated to insure the full payment of compensation when due," equally specific authority is not given to require methods that will prevent improper payments. The Council has proposed that this situation be corrected.

The Federal Government has a particular responsibility for the protection of employees who move from State to State. In both war and peace, it is important that people should be free to move and that those who move should not be discriminated against either in regard to their benefit rights or their right to prompt payment. The Council proposes the establishment of Federal provisions to assure the coordination of the individual State laws in such cases.

### ***Disqualifications***

The Council believes that the Federal interest requires the establishment of a standard on disqualification provisions. In 22 States employees who are disqualified not only are denied benefits for unemployment immediately resulting from the voluntary quit, refusal of suitable work, or discharge for misconduct, but also lose accumulated benefit rights which would otherwise be available to them if they are subsequently employed and suffer a second spell of unemployment. The Council can see no justification for these punitive provisions in a social-insurance program and recommends that they be prohibited. Federal action is apparently needed to correct this situation, since the number of States with such provisions has been increasing. In 1937, 7 States reduced or canceled benefit rights for causes other than fraud or misrepresentation; in 1940, 12; and in 1948, 22.

The Council also believes that the postponement of benefits as the result of a disqualification should be for a limited period only and recommends a period of 6 weeks as the maximum. This is probably the longest period during which it is reasonable to presume that the original disqualifying act continues to be the main cause of unemployment. The Federal standard should also prohibit interpretations of "misconduct" which tend toward making inability to do the work a basis for a finding of misconduct.

### ***Study of Supplementary Plans***

The State-Federal system of unemployment insurance should pay benefits of sufficient duration to permit most covered workers in normal times to find suitable employment before their benefit rights are exhausted. Furthermore, the Council has recommended that the State-Federal public-assistance program be strengthened to meet more adequately the needs of unemployed workers ineligible for insurance benefits or with inadequate insurance rights.<sup>5</sup>

These dual provisions for the unemployed through the State-Federal programs would suffice, the Council believes, unless the country is again plunged into a period of severe economic distress. In that event, additional Federal action would clearly be needed for the relief of the unemployed. A depression has an uneven impact upon different cities and regions, and many States and localities are not capable of meeting the greatly increased expenditures necessitated by mass unemploy-

<sup>5</sup> Recommendation 2 in the public assistance report provides for Federal grants for "general assistance." See p. 108.

ment. In such a period only the Federal Government has sufficient credit and sufficiently broad eventual tax resources to meet the full need.

The Council has not been able to make a thorough study of the alternative lines of action open to the Federal Government for providing income maintenance for the unemployed in such a situation and has therefore made no specific recommendations on this point. We recommend, however, that the Congress should direct the Federal Security Agency to study in consultation with other interested agencies various methods for providing income security for workers who do not have private or public employment and to make specific proposals for putting the best methods into effect.

### ***Temporary Disability Insurance***

The Council has also been unable to devote the time necessary for making policy decisions in the field of temporary disability. We have included in this report, however, a section which discusses the need for protection against wage loss due to illness and the methods that have been suggested by various groups to provide this protection.

### ***Importance of a Broad Informational Program***

No social-security program can be effective unless those who are entitled to participate know their rights and obligations. A program of public information is particularly important in unemployment insurance. In this program, with its necessarily somewhat complicated provisions, it is of great importance that all claimants and workers understand the principles of the program and the specific provisions of law. We believe that much remains to be done to develop an informed public through informational programs. The addition of an employee contribution and the greater use of advisory councils will also contribute to this end.

## RECOMMENDATIONS ON COVERAGE

### 1. Employees of Small Firms

*The size-of-firm limitation on coverage in the Federal Unemployment Tax Act should be removed, and employees of small firms should be protected under unemployment insurance just as they are now protected under old-age and survivors insurance*

In an average week of the year ended June 30, 1948, an estimated 3.4 million persons were excluded from unemployment insurance coverage under State laws because they were working for small firms. The need of these employees for unemployment insurance has been recognized from the beginning of the program. The size-of-firm restriction in the unemployment insurance titles of the original Social Security Act, limiting tax liability to employers with eight or more employees in each of 20 weeks during the year, was adopted as a temporary provision to simplify administration in the early years of the program. Experience under the old-age and survivors insurance program and under the unemployment insurance laws of 17 States, including such major industrial States as Pennsylvania, California, and Massachusetts, however, has now demonstrated the administrative feasibility of collecting contributions and wage records from small firms.

In 10 jurisdictions with widely differing economic characteristics—Arkansas, Delaware, District of Columbia, Hawaii, Idaho, Minnesota, Montana, Nevada, Pennsylvania, and Wyoming—employees of small firms have been covered since 1937. No serious administrative difficulties have been experienced. The seven additional States which now cover employers of one or more persons have also found such coverage to be administratively feasible. In fact, the administrative advantages of extension of coverage to small firms are probably greater than the administrative difficulties. For example, with the size-of-firm restriction removed, the State no longer faces the need for liability audits, or for questioning the employer about exact pay-roll counts. Some States have also found that having the same coverage as under old-age and survivors insurance facilitates policing tax liability by clearance with the Federal collector of internal revenue.\*

The number of workers excluded from the Federal Unemployment Tax Act in 1948 was substantially higher than the 3.4 million excluded under State laws, because only 22 States restricted coverage in that year to persons who worked for firms employing 8 or more workers. Of the other 29 States, 2 covered those working for firms employing 6 or more; 8 covered those working for firms with 4 or more; 2 covered those working for firms with 3 or more; while 17 covered those working for firms employing 1 or more. On the basis of 1946 data, the number of workers with wage credits under State unemployment insurance

\* Not all these 17 States cover employers of 1 or more at any time as in old-age and survivors insurance; in 6 States coverage is based solely on size of pay roll in a specified period; in 5 States employment must extend for a specified period.

laws would be larger by about 8.2 percent if the size-of-firm exclusion were removed. In the 22 States which retain the limitation in the Federal Unemployment Tax Act, the percentage increase in the number of workers with unemployment insurance wage credits would range from 11.6 percent in North Carolina to 35.1 percent in North Dakota, and would be more than 15 percent in half these States. Benefit rights of many persons who work for more than one employer would be greater because, in determining their rights, wages earned in employment for small firms would not be ignored as at present, but would be added to wages earned with large firms.

Twenty-nine State laws already contain provisions which will automatically broaden their coverage to the extent that the Federal size-of-firm limitation is reduced. (See table 2, appendix IV-E, for size-of-firm restrictions in State laws.)

## 2. Employees of Nonprofit Organizations

*The Federal Unemployment Tax Act should be broadened to include employment by all nonprofit organizations, except that services performed by clergymen and members of religious orders should remain excluded.<sup>7</sup> The exclusion of domestic workers in college clubs, fraternities, and sororities by the 1939 amendments to the Federal Unemployment Tax Act should be repealed so that these workers will again be protected under all State laws*

This proposal would broaden the coverage of unemployment insurance by bringing in approximately 1 million workers now excluded from protection because they are employed by nonprofit organizations. Almost one-half are in the service of charitable organizations, one-fourth are in educational institutions, and another one-fourth are in religious institutions.

Most State laws have followed the nonprofit exclusion in the Federal Unemployment Tax Act, but a few States already cover some workers in nonprofit organizations. Hawaii's exclusion applies only to service performed by members of religious orders or ministers of the Gospel. In Idaho and Oklahoma the exclusion does not apply to scientific or literary organizations; Indiana does not exclude service of a commercial character commonly performed for profit even though performed for a nonprofit organization; and New York does not exclude humane societies or building-trade employees of nonprofit organizations. Tennessee now limits the exclusion to professors, instructors, teachers, and executives in educational institutions, priests, clergymen, pastors, church musicians, singers, and members of choirs.

The extension of coverage to employees of nonprofit organizations presents no serious administrative difficulties; and the need of the great majority of these workers for unemployment insurance protection is clear. A very large proportion of the employees in charitable institutions work in hospitals which have relatively high employment turnover rates. Educational institutions—including not only schools but also private libraries and miscellaneous research agencies and civic groups—have considerable turn-over among younger instructors and custodial staffs, and secular employees of religious institutions also

<sup>7</sup> Two members of the Council favor extension of coverage to the nonprofit group on an elective basis. In substantial part, the reasons which they gave in their dissent in pt. I are applicable here (see appendix I-E, p. 63).

suffer from unemployment. Equity and adequacy of protection can be assured only when all individuals similarly situated are similarly protected. The laundress and the cook in a hospital have the same need for protection as those who work in a hotel; there is no essential difference between the janitor in a private school and the one in a retail store, or the elevator operator in a YMCA and the one in a glass factory.

Although some categories of workers for nonprofit organizations doubtless have a high degree of security in employment—as is also true of some in private profit-making institutions—the Council believes that this fact does not justify their exclusion. In a social program such as this, the indirect benefits to all justify exacting a minimum contribution even from those who are in relatively little danger of becoming unemployed.

The Council is aware of the difficulties of adequately financing nonprofit organizations and would be reluctant to have their costs increased for any less compelling reason than the protection of their employees. These costs should be kept at a minimum. Under the Council's proposals, the employers' contribution rate required by the Federal Government would be 0.75 percent of pay roll (recommendation 9, p. 166) regardless of the length of time the employer is subject to the act. At present the Federal Government requires a rate of 3 percent for an employer's first 3 years under the program. Furthermore, under recommendation 11, if a State wished to charge more than the minimum, it would, nevertheless, be prohibited from charging a rate for newly covered and newly formed firms which exceeded the average rate for all employers in the State.

With other college employees covered, there seems to be no reason to continue the exclusion of domestic workers in college clubs, fraternities, and sororities. These workers were protected until 1940 and, in the Council's opinion, protection should be restored to them.

The Council believes, however, that the present exclusion of services for organizations exempt from Federal income tax when the remuneration does not exceed \$45 per quarter should be continued. This exclusion would avoid much of the administrative difficulty of attempting to cover such persons as church singers and musicians and part-time semivolunteer workers for church and welfare organizations who, in any event, would usually not earn enough from the work to qualify for benefits.

The original exclusion of nonprofit employment was not based on the conviction that employees of nonprofit institutions needed protection less than others; it resulted from the fear of some institutions that they might lose their tax-exempt status, and the fear of some religious groups that they might become subject to some form of Government control. The Council, in considering the exemption of the same group from old-age and survivors insurance, stated its belief that extension of coverage under social insurance would not lead to the results feared. The statement made in connection with old-age and survivors insurance is equally applicable to unemployment insurance:

The members of the Council are unanimous in believing that freedom of religion should be protected, but we are convinced that a tax on employment—a function which employers in the nonprofit area have in common with all others—for the special purpose of giving equal social insurance protection to all employees

would in no way imply or lead to Government control over the performance of the religious function. To make it absolutely clear that the legislation is not concerned with the performance of religious duties, we recommend that persons directly engaged in religious duties, such as clergymen and members of religious orders, remain exempt from coverage under the program. Our recommendation would extend coverage only to lay personnel who perform services which are secular in character.

We also believe that public encouragement of religious, charitable, scientific, and educational enterprise should be continued through preservation of the traditional tax-exempt status of such institutions. That encouragement, however, would be better expressed, we believe, by extending social insurance protection to their employees than by continuing to deny it. Employers in the nonprofit field are at a considerable disadvantage in the labor market because they cannot offer retirement and survivorship protection, hence, coverage exclusion handicaps these organizations and fails to promote their services to the community.

Religious, charitable, scientific, and educational organizations, which have been traditionally exempt from taxation on income and property dedicated to the purposes which the community wishes to promote, can and should continue to enjoy their traditional tax exemption when the old-age and survivors insurance program is extended to their employees. It has long been customary to require such institutions to pay certain types of special assessments for property improvement, to pay Federal excise taxes, and in some States to pay the local and State taxes on commodities which they use. Even in some States with exclusive State funds, they have been required to carry workmen's compensation insurance. The use of Government compulsion in connection with these special taxes and levies has not led to taxation on the property and general income of these institutions. Moreover, many organizations such as trade-unions, trade associations, fraternal and beneficial organizations, and the like, which are exempt from the Federal income tax and certain other taxes, pay the old-age and survivors insurance contribution without appearing to be in danger of losing their exemption under other laws.<sup>8</sup>

The State unemployment insurance laws levy a special-purpose tax on the function of employment. The proceeds are automatically deposited in a trust fund dedicated to the payment of benefits to covered workers. Under recommendation 13, p. 172, the proceeds of the Federal Unemployment Tax Act will also be dedicated to unemployment insurance. Unemployment insurance taxes are a special kind of tax which should not serve as a precedent for other forms of taxation any more than would a special assessment levied by a local government. We believe, moreover, that Congress should indicate its intent that the taxation on nonprofit organizations for social insurance in no way implies a departure from the principle of promoting the function of these organizations through tax exemption.

### 3. Federal Civilian Employees

*Employees of the Federal Government and its instrumentalities should receive unemployment benefits through the State unemployment insurance agencies in accordance with the provisions of the State unemployment insurance laws. The States should be reimbursed for the amounts actually paid in benefits based on Federal employment. If there is employment under both the State system and for the Federal Government during the base period, the wage credits should be combined and the States should be reimbursed in the proportion which the amount of Federal employment or wages in the base period bears to the total employment or wages in the base period. The special provisions for Federally em-*

<sup>8</sup> See pp. 19-20.

*ployed maritime workers should be extended until this recommendation for covering all Federal employees becomes effective*<sup>9</sup>

The Council believes that the approximately 1.7 million employees of the Federal Government, now without unemployment insurance protection, should be covered immediately. A civil-service system in itself provides no guaranty against unemployment; separations among civil-service employees in recent years (1944-47) have ranged from 36 to 55 percent annually, and on the average somewhat more than half have been involuntary. Although these rates may be somewhat higher than may be expected in the future, they are nevertheless an indication that Federal workers are subject to a considerable amount of involuntary unemployment. The abolition of agencies or functions, reorganization of agencies, and reduction in appropriations, as well as the discharge of temporary or probational employees, are all common causes of unemployment among Federal workers, and indicate a real need for unemployment insurance.

In the Council's opinion, the Federal Government should offer its employees the same protection that it requires employers to provide in private industry. By so doing, the Government will not only fulfill its obligation as a good employer, but will also cease to handicap itself in a competitive labor market by offering less income protection against unemployment than private industries offer.

In recommending protection under unemployment insurance, the Council has considered whether other programs give the Federal worker sufficient protection against the risk of losing his job. It might be argued that the refunds paid under the Civil Service Retirement Act to those who have served less than 5 years in the Federal Government are a substitute for unemployment insurance. The Council is not of that opinion. Refunds to these short-time workers are usually very small and, in any event, represent withheld savings. Under State unemployment insurance laws for commercial and industrial workers, similar payments would not generally be considered in determining whether benefits are payable. While Federal employees with service of 5 to 20 years may, if they desire, receive substantial refunds, the Council believes that encouragement of such withdrawals would be unsound social policy. It would weaken the protection these workers had accumulated against the risk of old age to give them protection against the risk of unemployment. The Council's recommendation for the extension of unemployment insurance to Federal workers would make it unnecessary for them to cash in their retirement benefit rights to meet the immediate and pressing expenses of unemployment.

Similar considerations apply to an evaluation of accrued annual leave as a substitute for unemployment insurance. The annual-leave system is designed to promote the efficiency of the service, and Federal employees are expected to use the leave privilege as they are able. It would be unsound policy to encourage persons to forego vacations so that their accumulated annual leave will afford protection against the risk of unemployment.

In the Council's opinion, the extension of unemployment insurance under the State programs on a reimbursable basis is the most effective

<sup>9</sup> Two members of the Council favor protection of Federal employees under a Federal system with benefit and eligibility conditions established by Federal law and administered by the State organizations on a reimbursable basis.

and economical way of providing the protection needed by Federal workers. Coverage under the State programs will avoid treating Federal employees as a distinctive class and will give the same degree of protection to all workers seeking employment in the same localities. Employees of the same Federal agency will, of course, have differing benefit rights, depending on the law of the State in which they file their claims, just as is now true of persons employed by private firms with branches in more than one State. Such differences are inherent in a State-operated system.

Federal employment should be combined with employment covered under the State law to determine eligibility and benefit rights. The Federal Government should reimburse the State in the proportion which the amount of Federal employment or wages in the base period bears to the total employment or wages in the base period. Administrative expenses incurred by the States for benefits to Federal employees should be covered by the regular administrative grants.<sup>10</sup>

To reduce to a minimum the volume of interstate claims which would result from this proposal, the Council recommends that the State law applied to a Federal worker's claim be either the law of the State of his residence at the time of filing or the State in which he was last employed—the choice to be made by the employee. Federal workers who have served in foreign countries will thus be able to claim benefits based on the law of the State in which they are currently residing.

The Council recommends that benefits to Government workers who become unemployed be financed by direct reimbursement of the State agencies making these payments, rather than by State-imposed taxes. This is the plan now used for paying unemployment-insurance benefits for former employees of the War Shipping Administration, and it seems more practical than any other for those who have been employed by the Federal Government in more than one State or have been employed abroad. Furthermore, if the Federal Government were to pay "contributions," like any other employer, either the State system would bear part of the load for the Federal Government or the Federal Government would pay part of the costs of unemployment for all workers. The Council believes that the Federal Government should not use a method of that type to support State unemployment-insurance funds. Federal employees should contribute at the minimum rate required by the Federal Government for all covered employees (recommendation 7, p. 163). The contribution should be collected by the Federal Government and used in the reimbursement of the States. Additional amounts necessary to cover the cost of benefits actually paid should be appropriated from the general revenues of the Federal Treasury.

This recommendation would require the Social Security Administration to enter into agreements with State agencies to handle the claims of Federal workers. If such an agreement is not reached in a State, the Social Security Administration should be empowered to pay the benefits in that State on the same terms as if the agreement were in effect. In working out the agreement, the States should permit the Federal Government to limit its wage reporting to wage-and-separation reports for individuals who are separated or who apply for

<sup>10</sup> It would be desirable for Congress to add to the total funds dedicated to unemployment insurance and available for administration (0.3 percent of covered pay rolls, see recommendation 13, p. 172) by appropriating an additional amount estimated to cover the costs of administering the program for Federal employees. It does not seem practicable to make special grants to the individual States covering these costs alone.

benefits. A similar right is now granted to large employers by some States, and Wisconsin and Michigan use this method for all employers.

In 1946, the Federal Unemployment Tax Act was amended to permit State laws to cover seamen on private vessels and to provide a temporary reconversion unemployment benefit for seamen employed by the United States Maritime Commission. Under the present shipping situation, the Maritime Commission will operate longer than anticipated. The special provisions for federally employed maritime workers should therefore be extended until this recommendation for covering all Federal employees becomes effective. Thereafter, the special provisions for maritime workers should be terminated.

#### 4. Members of the Armed Forces

*Members of the armed forces who do not come under the servicemen's readjustment-allowance program should be protected by unemployment insurance*

At present, members of the armed forces with service between September 16, 1940, and July 25, 1947, are protected by the Federal servicemen's readjustment-allowance program, under which unemployed servicemen may receive a flat weekly benefit of \$20 for as many as 52 weeks. This protection will expire for most servicemen on July 25, 1949.<sup>11</sup> The benefits are administered by the State agencies responsible for the administration of the State unemployment-insurance laws, and the law of the State in which the claim is taken governs the criteria used for determining suitable work.

The servicemen's readjustment-allowance program was designed for those who served in the armed forces in time of war. In our opinion, many of its provisions are not appropriate to peacetime service in the Army and the Navy. The flat duration of 52 weeks, for example, now permitted for World War II veterans, seems inappropriate for persons serving only the 21-month period required under the current draft. Yet, those who serve in the armed forces in peacetime, like any other employed group, need protection against the risk of unemployment. Some ex-servicemen will readily find a place in industry, but others will need a longer period in which to get jobs. Unemployment insurance is the most satisfactory way of giving the needed protection. Unlike a dismissal payment which would be the same for all, the insurance program pays benefits only as long as the man is unemployed, thus using available funds where they are most needed.

The Council believes, therefore, that protection against the risk of unemployment should be extended on a permanent basis to those who serve in the armed forces, and that the insurance program for servicemen should be based on peacetime conditions. As a matter of public policy, service in the armed forces should be made more attractive than it is now. One method would be to grant social-insurance rights for military service just as such rights are granted for employment with private industry. The Council has considered two possible approaches, either of which is satisfactory to the majority of the Council, although some prefer one and some the other. One way of extending unemploy-

<sup>11</sup> Allowances may be claimed for any week ending on or before July 24, 1949, or 2 years after date of discharge, whichever is later (but not later than July 24, 1952), except that persons enlisting or reenlisting in the armed forces between October 6, 1945, and October 5, 1946, under the Armed Forces Voluntary Recruitment Act of 1945, may receive benefits during a limited additional period.

ment-insurance protection to the armed services would be to establish a Federal system which would be administered by the State agencies, following the pattern established by the servicemen's readjustment-allowance program. The Federal act would determine the eligibility conditions, the benefit amount, and the maximum duration, while the States would actually administer the program and apply State law to the determination of suitable work. Under this plan, as under the readjustment-allowance program, the benefit rate would probably be the same for all regardless of previous rank.

The other approach is to treat members of the armed forces as we propose to have all other Federal employees treated (recommendation 3, p. 156). Under this plan State law would determine the eligibility conditions, benefit amount, duration, etc.; benefits would be based on actual wages paid, including the fair value of board and clothing,<sup>12</sup> and would vary with the serviceman's grade. The Federal Government would reimburse the States for unemployment-insurance benefits paid under this program and would pay the cost of administration in the same manner as for other Federal employees.

Under either of these plans, the Council believes, members of the armed services should contribute toward the cost of their protection like other employees (recommendation 7, p. 163). The contributory principle should apply to all, and servicemen should have the same interest and stake in the system as other covered workers.

## 5. Borderline Agricultural Workers

*To afford protection to certain workers excluded by the 1939 amendments to the Federal Unemployment Tax Act, defining agricultural labor, coverage of that act should be extended to services rendered in handling, packing, packaging, and other forms of processing agricultural and horticultural products, unless such services are performed for the owner or tenant of the farm on which the products are raised and he does not employ five or more persons in such activities in each of four calendar weeks during the year. Coverage should also be extended to services now defined as agricultural labor by section 1607 (1) (3) of the Unemployment Tax Act.*

In an average week, approximately 1.7 million individuals are unable to acquire unemployment-insurance protection because they are agricultural workers, and at some time during a year as many as 4.1 million are employed in work defined as agricultural. In the Council's opinion, extension of coverage to these workers under the unemployment-insurance program—the Federal Unemployment Tax Act and State unemployment-insurance laws—is highly desirable. From the viewpoint of the objectives of the program, the agricultural workers' need for protection is unquestionable. Their employment is unstable, and their wages are often too low to permit them to accumulate savings to tide them over periods of unemployment. Moreover, as surveys of the employment history of farm workers show, the number of persons with both farm and nonfarm employment in the course of a year is appreciable. Since much of their nonfarm employment is covered, these workers frequently claim unemployment-insurance benefits. If all their work were covered, a higher proportion of them

<sup>12</sup> The Army estimates board and clothing to be worth \$108 a month at 1948 prices.

would be eligible for benefits, and the benefit rights of those now eligible would be increased.

The Council, however, does not recommend at this time extension of the Federal Unemployment Tax Act to all agricultural employment. Such an extension would in effect require the States to cover all agricultural workers immediately, and the Council recognizes that certain administrative problems connected with extension of coverage to this group would present serious difficulties in some States. While problems of reporting wages and collecting contributions are similar to those in old-age and survivors insurance, unemployment insurance has an even greater need for prompt and accurate reporting. Since unemployment-insurance benefits are usually based on recent wages paid during a relatively short period, rather than a lifetime average, an error or delay in reporting may have a far more serious effect on benefit rights in unemployment insurance than in old-age and survivors insurance.

The Council recommends, however, immediate extension of the Federal Unemployment Tax Act to those persons now excluded by section 1607 (1) (3) and those excluded by section 1607 (1) (4) who are engaged under what are substantially commercial conditions in the handling, grading, storing, packaging, delivery to storage or to market, and other processing of agricultural products. Both of these groups were originally covered under the Federal Unemployment Tax Act and were excluded by the amendments of 1939. The packaging and processing group is made up of some 200,000 to 225,000 persons, many of whom are covered under State, although not Federal, law. For example, Florida covers the grading, packing, packaging, or processing of fresh citrus fruits; and California restricts the agricultural exclusion to services on a farm or in the employ of the owner or tenant of the farm where the materials being processed were produced. A number of States require that the service to be excluded must be for an owner or tenant as an incident to ordinary farming operations. The laws of 32 States, however, follow the Federal definition and exclude nearly all workers engaged in packing and processing agricultural products, other than in commercial canning and freezing.

The Council believes that the continued exclusion of this group by the Federal law is unjustified. These persons frequently work under factory conditions and operate mechanical equipment such as graders or conveyors. Stationary engineers tending steam boilers, box assemblers, truck operators, plant superintendents and department foremen, receiving clerks, box ladders, electricians, and mechanics are excluded, as well as the workers who handle, sort, grade, wash, polish, and pack the fruits and vegetables, and the laborers who keep the packing house in order. The operations which these workers perform are essentially commercial or industrial in character.

The Council believes, on the other hand, that when packing and processing services are not essentially a commercial operation but are performed in the employ of the owner or tenant of a small farm, these services should remain excluded until coverage is extended to all farm workers. The Council recommends that the farmer who does not employ at least five persons in packing and processing work in each of four calendar weeks during the year should not be subject to the act. Services of this nature performed for persons other than the owner

or tenant of the farm growing the products to be processed would be covered without exception.

Section 1607 (1) (3) of the Unemployment Tax Act excludes services performed off the farm in connection with the ginning of cotton; the hatching of poultry; the operation or maintenance of ditches, canals, reservoirs, or waterways used for supplying and storing water for farming purposes; and in connection with the production and harvesting of maple sirup or maple sugar, turpentine, gum resin, and crude gum. These activities are not what one ordinarily means by agricultural labor and, in our opinion, should be covered under the Federal act. The Council believes that the test should be whether the employment is reasonably associated with industry now covered and whether it can be brought under the program without substantial administrative difficulty. If performed on a farm, these activities would ordinarily continue to be excluded by the definitions in sections 1607 (1) (1) or 1607 (1) (2).

The Council hopes that some of the States will take advantage of the opportunity to assume leadership in extending coverage to a larger part of farm employment than we feel should be covered immediately under the Federal act. Under the State-Federal program, States wishing to make progressive changes can take such steps before it seems practical to require such changes in all States. States might experiment with several possible approaches to extending coverage to a part of the group of farm workers. Two approaches which seem to be among the most promising are:

1. Extension of coverage to all those working on farms with more than a given number of workers, for example, four; or
2. Extension of coverage to all employees of farm operators with an annual pay roll in excess of a specified amount.

## 6. Inclusion of Tips in the Definition of Wages

*The definition of wages contained in section 1607 (b) of the Federal Unemployment Tax Act should be amended to specify that such wages shall include all tips or gratuities customarily received by an employee from a customer of an employer*

Tips or gratuities paid directly to an employee by a customer of an employer, but not "accounted for" by the employee to the employer, are not now included in wages as defined under the Federal Unemployment Tax Act. Moreover, relatively few tips are accounted for and subject to the Federal law. As many as 31 States, however, levy unemployment-insurance contributions on tips without differentiating between those accounted for and others. In the absence of an exact reporting by persons receiving tips, most of these States permit employers to report a reasonable estimate of the amount received as tips by their employees. In making such estimates, the employer takes into account the volume of business handled by the employee, the tips reported by other employees, the type of establishment, and other pertinent factors. In many instances, such estimates are made after agreement with the employee. Although the administrative problems connected with the inclusion of tips are not inconsiderable, they are generally being solved satisfactorily and are not substantial enough to justify the continued exclusion of this type of remuneration from the Federal law.

The Council believes that the Federal Unemployment Tax Act should be amended to include all tips in the definition of wages. In the absence of such an amendment, substantial numbers of workers in some States—those employed in restaurants, barber shops, beauty parlors, and the like—are denied the degree of protection they would acquire if their tips and gratuities were included in their wage records. Some workers may fail to qualify for unemployment benefits because, except for tips, they receive inconsequential remuneration. This situation is especially illogical because tips are frequently contemplated in the wage contract, are earned in the service of the employer, and are received for services generally recognized as performed in the interest of the employer.

The Council has recommended identical provisions for old-age and survivors insurance. From an administrative standpoint, it is highly desirable to have an identical tax base in both systems of social insurance. Tips are also included as taxable income under the Federal income-tax law.

While the Council urges that all tips be included for tax and benefit purposes either on an estimated or reported basis, it believes that—if the reporting basis is chosen—the employer should be protected from inaccuracy on the part of his employees. The Council believes that employees should not be allowed to change a previous report on tips when applying for benefits. Otherwise, additional assessments would have to be levied against the employer or benefits would be paid at rates higher than contributions collected would warrant. The Council considers both these results undesirable.

## RECOMMENDATIONS ON BENEFIT FINANCING

### 7. Contributory Principle

*To extend to unemployment insurance the contributory principle now recognized in old-age and survivors insurance, a Federal unemployment tax should be paid by employees as well as employers. Employee contributions to a State unemployment-insurance fund should be allowed to offset the Federal employee tax in the same manner as employer contributions are allowed to offset the Federal tax on employers. The employee tax would be collected by employers and paid by them when they pay their own unemployment tax*

The Council believes that part of the cost of social-insurance programs should be borne directly by those who are the beneficiaries of the program. The employee contribution is a significant factor in public understanding, for it demonstrates the insurance principle and the worker's right to the benefit and clearly differentiates social insurance from relief and assistance. The contributory principle is recognized not only in old-age and survivors insurance program of this country but also in the unemployment-insurance laws of all other countries. It is a cornerstone of social insurance.

The Council recommends the addition of an employee tax in unemployment insurance because of the fundamental concern of employees with the operation of this program. They receive the benefits; they are greatly affected by the administration of the laws; and they have a basic interest in determining legislative policy.

Employee interest in administration would be strengthened by employee sharing in the cost of the program. If they paid part of the cost directly, employees would have an even greater stake than at present in promoting methods of administration which will best assure the full exercise of their rights to benefits and the prompt payment of those benefits. An employee contribution would also stimulate employee interest in the prevention of improper payments, whether due to lax administrative procedures or to fraudulent claims, for they will want to avoid having their contributions dissipated unwisely. Students of British experience cite many instances in which labor representatives were better able to prevent abuses than were employers or officials.

Labor now complains that some State legislatures listen more attentively to employer groups than to those representing employees, because the unemployment-insurance program is considered by many to be financed exclusively by the employers. The employee tax would help put employees on a parity with the employer. On the one hand, if employees pay a part of the cost they will have a stronger voice in determining the amount of benefits and the conditions of eligibility; on the other hand, their direct contribution should make employees more responsible in their demands for higher benefits than if the cost falls on them only indirectly. Under the present arrangement, many employees believe that benefit increases are financed entirely by the employer and they tend therefore to exert their influence mainly toward payment of higher benefits without consideration of costs.

Since some of the employer's tax is shifted to the workers as employees and as consumers anyway, it would be far better to tax workers directly and achieve the advantages to be derived from the recognition of their part in paying the costs of benefits. Under the present law employers can shift at least part of the unemployment taxes to the consumer in higher prices or to the worker in lower wages. In good times, the former is more feasible, while in times of unemployment the latter is more likely to occur.

Only two States, New Jersey and Alabama, now provide for employee contributions to unemployment insurance, although nine States have required such contributions at one time or another. Federal action is needed to extend the contributory principle in unemployment insurance to all States. At the same time section 303 (a) (5) of title III of the Social Security Act should be revised to provide that, after the effective date of a Federal unemployment tax on employees, the employee contributions available for temporary disability benefits should be limited to the amount in excess of the minimum rate required for unemployment insurance. Employee contributions paid into the unemployment trust fund before that effective date would continue to be available for the State's disability-insurance program.

Following the principles of the present State-Federal program, employee contributions to a State unemployment-insurance fund should be allowed as an offset against the Federal employee tax in the same manner as offsets are allowed against the Federal tax on employers. The employee tax would be withheld by the employer from wages and combined with the amount he is required to pay as an employer. Federal employees should contribute at the minimum rate required by the Federal Government for all covered employees but, in accord-

ance with recommendation 3, the contribution would be collected by the Federal Government and used to reimburse the States for benefits actually paid on the basis of wage credits earned from Federal employment.

### 8. Maximum Wage Base

*To take account of increased wage levels and costs of living, and to provide the same wage base for contributions and benefits as that recommended for old-age and survivors insurance, and upper limit on earnings subject to the Federal unemployment tax should be raised from \$3,000 to \$4,200*<sup>13</sup>

A social insurance program must be adjusted periodically to basic economic changes. In a dynamic economy, some provisions which were appropriate when they became effective eventually become outmoded. This is what has happened to the limitation placed on the amount of annual wages subject to social insurance contributions.

In 1939, when the maximum wage base for contributions and benefits was set at \$3,000, nearly 97 percent of all workers in covered employment had wages of less than \$3,000 a year; contributions were thus paid on the full wages of virtually all covered workers. With the general rise in wage levels since 1939, however, the \$3,000 limitation has tended to exclude from taxation part of the wages of a substantial proportion of covered workers. In 1947 about 18 percent of all covered workers had wages exceeding \$3,000, and among workers who were steadily employed throughout the year, from one-fourth to one-third had wages in excess of that amount. When the figures for 1948 are available, these percentages will be even higher.

As wages continue to rise, the \$3,000 limitation excludes a larger and larger proportion of wages from taxation. Thus the system suffers progressive loss of income, which makes it increasingly difficult to finance benefits related to current wages. Furthermore, when the limitation excludes a significant part of the wages, it is a source of inequality in the tax burden, for the ratio of taxes to wages is lower for establishments with high average wages than for those with low wages. In our opinion, the taxation base should be kept broad and the tax rate set lower than would be prudent with a more limited base.

The higher wage base is not only wise for revenue purposes but is also desirable as a base for calculating benefits. In a contributory system, taxes should be paid on all wages which serve as a basis for benefits. It is undesirable, for example, to pay higher benefits to those getting more than \$3,000 than to those at the \$3,000 level without at the same time charging more for the higher benefits. Thus if wages in excess of \$60 a week (approximately \$3,000 a year) are

<sup>13</sup> While the majority of the Council favor increasing the upper limit to \$4,200, some favor keeping the limit at \$3,000 and some favor increasing it to \$4,800. Those who favor the retention of the present tax base feel that adequate benefits can be paid without any change and cite as evidence the benefits already being paid by several States, such as New York and California. An increase in the base would result in an increase in benefits only to those in the upper income group. In the opinion of these members, payment of increased benefits to this group is not consistent with the basic principle of social insurance to provide a basic floor of protection. Those who feel that the change in the top limit of taxable wages should be to \$4,800 rather than \$4,200 accept the reasoning of the majority report, but point out that the consumers' price index has risen by more than 60 percent, so that an income of \$4,800 today has less purchasing power than an income of \$3,000 had in 1939. Hence, raising the tax base and wages credited for benefits to \$4,800 would not be a real increase—it would, in fact, fall short of maintaining the 1939 relationship between the wage base and prices. In substantial part, the reasons which were given by both groups in their dissents in pt. I are applicable here. See appendix I-F, p. 64.)

credited for benefit purposes, the tax base should be similarly increased. To relate benefits to wages for a large proportion of claimants, benefits should be based on wages above this \$60 a week figure. If benefits are to vary with earnings for even as many as three-fourths of the claimants and if workers are to receive as much as 50 percent of earnings, in many States benefits would now have to be based on earnings up to \$70 or \$80 a week. If wages continue to rise, more and more States will be in this position.

The Council believes that a system of differential benefits related to the individual's contribution to production as reflected in his earnings supports general economic incentives and provides more adequate security than does a system which fails to take account of the individual's standard of living. The desire to return to productive work is well protected by a system which relates benefits to the earnings of the individual worker. Such a system permits higher benefits to those who are able to earn more and consequently, while protecting the desire to return to work, compensates for a greater proportion of total wage loss due to unemployment than is possible under a system in which a large proportion or all of the beneficiaries receive the same amount. For these reasons we believe it is important that, in the great majority of cases, benefits should vary with the wages earned by the individual worker and that the system should not become a flat benefit system because of benefit maximums which are too low in relation to current wages.

To take full account of increases in wages and prices, the limitation on taxable wages would have to be raised to somewhat more than \$4,800. The Council, however, recommends that a part of the increase in wages be disregarded by raising the limit to \$4,200 as a conservative adjustment to the rise in wage and price levels which has occurred since the \$3,000 limitation was adopted. The \$4,200 limitation proposed for unemployment insurance is the same as that recommended by the Council for old-age and survivors insurance. For administrative reasons it is desirable to have the same contribution base for both systems.

### 9. Minimum Contribution Rate

*The Federal unemployment tax should be 0.75 percent of covered wages payable by employers and 0.75 percent payable by employees. The taxpayer should be allowed to credit against the Federal tax the amount of contributions paid into a State unemployment fund, but this credit should not exceed 80 percent of the Federal tax. Since no additional credit against the Federal tax should be allowed for experience rating, the States would, in effect, be required to establish a minimum rate of 0.6 percent on employers and 0.6 percent on employees*

The Council believes that Congress should put a floor under State unemployment contribution rates at a point which will allow the majority of States to pay adequate benefits to most unemployed members of the covered labor force for a period sufficient in normal times to cover the duration of their unemployment. Under the present law there is no floor under the rates which States may charge. Credit allowances against the Federal tax are permitted to replace actual tax payments for the full 90 percent offset, as long as the allowances are based

on experience rating. States may thus reduce their contribution rates to a very low average rate and even to zero for some employers. (See table 10, appendix IV-E, for average employer contribution rates 1941-48.)

The present arrangement permits the States to compete in establishing low contribution rates for employers and therefore discourages the adoption of adequate benefit provisions, since proposals to provide more nearly adequate benefits in a given State are weighed against the effect of increased contribution rates on the competitive position of employers in that State. Yet a basic purpose behind the State-Federal tax offset plan adopted in 1935 was to remove interstate competition. Until the passage of the Federal act, the States were reluctant to require unemployment insurance contributions from employers within their boundaries unless other States had similar requirements. The Council's proposed minimum contribution rate is a return to the principle of assuring relative equality among employers in the various States. It will remove an important barrier to the liberalization of benefits by requiring that all covered employers and employees throughout the Nation pay a minimum rate.

Some States will have to charge more than the minimum suggested by the Council if they are to finance an adequate system of benefits; others will be able to pay benefits somewhat higher than the amount used by the Council in deriving the suggested rate. This situation will result from the considerable differences among the States in the size of reserves and in the unemployment rates which may be expected to prevail. Under the Council's recommendation, each State will continue to be responsible for relating its contribution rates to its own benefit payments and reserves. A State could thus impose a higher rate on all employers and all employees, or it could maintain a system of experience rating under which some employers would pay more than the minimum rate.

The Council is aware that some jurisdictions, such as Wisconsin, Hawaii, and the District of Columbia, will have unusually low costs if their past benefit experience can be taken as a reliable guide. Under the minimum tax proposed, these governmental units can perhaps afford to pay more generous benefits than can other jurisdictions. If, in the future, any State with benefits substantially more generous than others continues to build up a reserve, the Congress might consider some adjustment in the minimum rates required of them or allow all or part of the minimum employee contribution in such States to be used for other social insurance purposes. The Council believes that no special plan is needed now to provide for such a contingency, and none may ever be needed.

Appendix IV-A discusses in detail the method of arriving at the minimum rate.<sup>14</sup> In general, it was necessary to assume certain illustrative benefit plans as "adequate" and then to estimate the cost of such plans in the various States. These costs were estimated under two widely differing hypothetical sets of economic conditions for the next 10 years, and the actual cost was assumed to fall within the resulting range.

<sup>14</sup> A comprehensive study of the principles underlying the estimates of unemployment insurance costs has been made by W. S. Woytinsky, formerly principal consulting economist to the Bureau of Employment Security of the Social Security Administration, *Principles of Cost Estimates in Unemployment Insurance*, Government Printing Office, Washington, 1948. This study has been the basis of the cost estimates used by the Council.

Since reserves in most States are now at a high level, we have assumed that a substantial part of the costs of benefits during the next 10 years should be met from these reserves. We have set therefore the minimum contribution rate at a point which will allow most States to pay adequate benefits if they utilize a considerable portion of their reserves. (See table 11, appendix IV-E, for funds available for benefits as of September 30, 1948.)

The present system of State offsets against the Federal tax should be continued, but the percentage should be changed from 90 percent to 80 percent. The employer and employee would thus have to pay a minimum of 0.6 percent each to the State and 0.15 percent to the Federal Government. Thus the present Federal income of 0.3 percent of pay roll would remain unchanged although it would now be paid in equal shares by employer and employee.

### 10. Loan Fund

*The Federal Government should provide loans to a State for the payment of unemployment insurance benefits when a State is in danger of exhausting its reserves and covered unemployment in the State is heavy. The loan should be for a 5-year period and should carry interest at the average yield of all interest-bearing obligations of the Federal Government*

The Council believes that during a period of heavy unemployment, the Federal Government should stand ready to make loans to States whose unemployment trust fund reserves are in danger of being exhausted. In times of relatively light unemployment, a State would be expected to raise its unemployment contribution rate to prevent exhausting its reserve. That remedy would not be justified, however, during a period of heavy unemployment when an increase in the contribution rate would aggravate unemployment and impose hardships on many employers and employees. Equally disastrous in a time of heavy unemployment would be an attempt to preserve solvency by reducing the amount or duration of benefits or by restricting eligibility. The Council believes that present provisions in several State laws which provide for a decrease in benefits or an increase in contribution rates when reserves fall below a given point are contrary to sound policy. To obviate need for such measures, we recommend the establishment of a Federal loan fund.

A State's need for a Federal loan may result from two causes:

1. The contribution rate established by a State may be too low to meet actual costs over the entire 10-year period. Since the volume and incidence of unemployment are difficult to predict and differ from State to State, some States will, through error, probably establish contribution rates too low to finance benefits. If they rely on the minimum rate set by the Federal Government (recommendation 9, p. 166), a few States will almost certainly find the rate too low to support an adequate benefit program over the cycle.

2. Although the rate may be sufficient to support the system over the cycle, the fund may be temporarily exhausted. It is expected that a State will establish a contribution rate designed to cover costs over a relatively long period, such as 10 years. This assumption was the basis used in determining the minimum contribution rate discussed in

recommendation 9, page 166, and appendix IV-A. Such a rate, however, is not expected to provide income equal to outgo during some phases of the business cycle. Thus States with unusually severe fluctuations in the level of employment or with relatively low initial reserves might temporarily lack funds sufficient to meet benefit costs.

If a State's need for the Federal loan results from the situation described under 2, the loan will be self-liquidating, because the State's unemployment contributions will in time yield sufficient revenue to repay the amount borrowed. But if the situation is that described under 1, the State will have to use other revenue sources or increase its unemployment contribution rate after the volume of unemployment has declined.

The Council is aware that some States have constitutional provisions which, unless amended, will prevent them from taking advantage of these loans. It seems important to us, however, that the Federal offer be put on a businesslike basis with provision for the payment of interest and other safeguards against too frequent and too extensive borrowing. The loan should be for a 5-year period and should carry interest at the average yield of all obligations of the Federal Government. This is the interest rate now paid to the States by the Federal Government on the amounts which the States have on deposit in the Unemployment Trust Fund. No one loan should be greater than the estimated requirements of the State for the next 12 months but there would be no limit on the total amount which a State might borrow. The State would become eligible for a loan on meeting all other conditions if it had insufficient funds in its unemployment trust fund account to meet estimated expenditures for the next 12 months.

To promote a more rational relationship between the contribution rates and the cyclical movements of business, it is desirable to prevent an increase in rates when unemployment is high. If a State increased its unemployment contribution rate before covered unemployment had dropped below a given percentage of covered employment in that State—an appropriate figure might be from 10 to 12 percent—further loans would be denied. To provide for prompt repayments of the loans, the Federal law should require that all contributions deposited in the State's unemployment trust fund account in excess of benefit payments expected in the next quarter would be applied against the loan. The loan should be negotiated by the Federal Security Administrator on application of the State agency and he would approve the loan for payment by the Treasury.

As indicated in recommendation 13, p. 172, the income from the Federal Unemployment Tax Act should be earmarked for unemployment insurance purposes, and one-half of any surplus over expenses incurred in the collection of the tax and the administration of unemployment insurance and the employment service should be appropriated and credited to the loan fund. The War Mobilization and Reconversion Act of 1944 has already established a fund to provide advances to the States for unemployment benefits, but, under existing law, that fund would terminate on April 1, 1950. By July 1948 that fund, which was authorized to hold the difference between the 0.3 percent Federal unemployment tax and the actual administrative expenditures of the State and Federal Governments under title III of the Social Security Act, would have totaled \$970,000,000 if the authorized appropria-

tion had been made.<sup>15</sup> The amount already authorized for this fund should stand to the credit of the new loan fund and should be appropriated as needed. If the amounts available from both these sources prove insufficient to finance the necessary loans, the additional sums needed should be appropriated from general Federal revenues.

### 11. Standards on Experience Rating

*If a State has an experience rating plan, the Federal act should require that the plan provide (1) a minimum employer contribution rate of 0.6 percent; (2) an employee rate no higher than the lowest rate payable by an employer in the State; and (3) a rate for newly covered and newly formed firms for the first 3 years under the program which does not exceed the average rate for all employers in the State*

To finance an adequate system of unemployment insurance, some States will need to establish unemployment contribution rates higher than the combined employer and employee minimums of 1.2 percent required by the Federal Government. In such cases, the Council believes that the States should be left free to set the higher rates uniformly for all employers and employees or to relate the higher employer rates to the employer's individual experience with the risk of unemployment. The Council believes, on the basis of its analysis of the arguments for and against experience rating, that the Federal interest in unemployment insurance does not require prohibition of all experience rating but is concerned rather that contribution rates reduced through experience rating are consistent with reasonably adequate benefit provisions and sound fiscal practice.

Under the Council's proposals for a minimum contribution rate (recommendation 9, p. 166), experience rating in most States could not operate to reduce the income of the system to a point which would threaten adequate benefit standards. Furthermore, the minimum rate would place a limit on the tendency of most experience rating plans to reduce contribution rates in prosperous times just when general economic principles dictate peak rates, and correspondingly would limit the increase in rates in periods of growing unemployment when it is desirable to have low rates. The Council believes that, after establishing certain safeguards, the Federal Government should leave to the States the option of maintaining experience rating plans.

A minimum employer contribution rate of 0.6 percent would be automatically achieved under recommendation 9, p. 166, hence no specific Federal standard on this point would be necessary. The Council proposes, however, two Federal standards for State experience rating plans to replace the present requirements in section 1602 of the Federal Unemployment Tax Act, which would become obsolete under the Council's proposal. These Federal standards are as follows: (1) The contribution rate for employees should not exceed the lowest rate payable by any employer in the State, and (2) newly formed or newly covered firms, for the first 3 years under the program, should be required to pay no more than the average rate for all employers in the State.

<sup>15</sup> This figure equals the 0.3 percent of pay roll collected by the Federal Government since 1936, minus the Federal costs of collecting the tax and administering the unemployment insurance program and all grants to the States under title III of the Social Security Act. Grants to the States under title III include the expenses of administering unemployment insurance for all years and the expenses of the employment service related to unemployment for the years 1938 through 1941.

The Council considers experience rating inapplicable to employees. Generally speaking, differentials based on company experience with the risk of unemployment could not be expected to stimulate employees to effective action in regularizing employment. In our opinion, all employees in a State should pay the same rate for the same benefits. We believe further that employees should not pay at a higher rate than their employers. It follows therefore that under experience rating schemes, the employee rate for all employees should equal the rate payable by the employer with the lowest rate in the State.

Under the present law, new employers must have 3 years of contribution experience before they are eligible for a reduction from the full 3 percent tax rate. Many new business ventures, especially firms established by veterans, have felt this provision discriminatory, since they must pay the full rate, while some of their long-established competitors may pay less than 1 percent. The mere repeal of section 1602 would allow the States to determine the rates payable by new employers and newly covered employers more equitably than is now possible; the Council nevertheless believes that the Federal Government should go further and require State experience rating plans to stipulate that new employers will be required to pay no more than the average contribution rate for all employers in the State for the first 3 years under the program. Under the proposed standard, a State would be allowed to charge new firms a lower-than-average rate, perhaps the minimum State rate of 0.6 percent.

## RECOMMENDATIONS ON ADMINISTRATION

### 12. Combining Wage Credits Earned in More Than One State and Processing Interstate Claims

*The Social Security Administration should be empowered to establish standard procedures for combining unemployment insurance wage credits earned in more than one State and for processing interstate claims. These procedures should be worked out in consultation with the administrators of the State programs and should provide for the combination of wage credits not only when eligibility is affected but also when such combination would substantially affect benefit amount or duration. All States should be required to follow the prescribed procedures as a condition of receiving administrative grants. Similar procedures should be worked out, in cooperation with the Railroad Retirement Board, for combining wage credits earned under the State systems and under the railroad system.*

In a State-Federal system, the Federal Government has a clear responsibility for seeing that the provisions of the several State unemployment insurance programs do not penalize workers who move from State to State in search of work. Of the 51 jurisdictions, 45 now have a limited type of voluntary interstate agreement on combining wage credits, but only if such combination is needed to make a worker eligible for unemployment benefits. No provision is made for combining credits solely to increase the benefit amount or duration and there is no safeguard to prevent the windfalls which may now result when a worker becomes entitled to benefits in more than one State. All States participate in a voluntary plan for the acceptance and transmittal

of claims based upon wage credits earned in other States. Under present arrangements, however, long delays in the payment of these claims frequently result from divided authority among the States. The State taking the claim gathers the facts, while the State in which the credits were earned makes all decisions. An appeal under these conditions is particularly difficult to process.

At present 18 States are engaged in an experiment in which the State where the wage credits were earned makes the initial decision only. All decisions on continuing eligibility are made in accordance with the law of the State in which the worker is applying for benefits.

The Council believes that it is possible to work out more equitable protection for the interstate worker and that all States should be required to cooperate in giving such protection. The absence of even one State as a party to these agreements leaves a serious gap in the protection afforded. At present, even the States that have entered into voluntary agreements may withdraw at any time or merely refuse to follow the procedures agreed upon if they find them onerous. In our opinion, the Federal Government, in protecting the interest of the interstate worker, cannot afford to rely on the voluntary cooperation of individual States. The Social Security Administration should be empowered by statute to prescribe standard procedures for combining wage credits earned in more than one State and for processing interstate claims. These procedures should be worked out in consultation with the administrators of the State programs. All States should be required to follow the procedures as a condition of receiving administrative grants.

The Council recognizes that Congress has long responded to the expressed need for special legislation for railroad workers and that unemployment insurance for such workers would be particularly difficult to administer under State laws, since a large proportion of railroad employment is performed in more than one State. The Council, in its consideration of the relationship of the old-age and survivors insurance program to the railroad retirement program, has noted, however, the large extent of shifting between railroad and other employment. The Council therefore strongly recommends that the Social Security Administration, the Railroad Retirement Board, and the State employment security agencies develop the provisions necessary for combining wage and employment credits for unemployment insurance that will neither penalize nor encourage shifts to or from railroad employment.

### 13. Financing Administrative Costs

*Income from the Federal Unemployment Tax Act should be dedicated to unemployment-insurance purposes. One-half of any surplus over expenses incurred in the collection of the tax and the administration of unemployment insurance and the employment service should be appropriated to the Federal loan fund and one-half of the surplus should be proportionately assigned to the States for administration or benefit purposes. A contingency item should be added to the regular congressional appropriation for the administration of the employment-security programs. The administrative standards in the Social Security Act should be applicable to the expenditure of the surplus funds as well as to expenditures of the funds originally appropriated*

Administrative costs of State unemployment-insurance programs and State employment services are now financed by grants to the States from the general revenues of the Federal Government. Individual States estimate their work loads on the basis of general economic assumptions supplied by the Social Security Administration. Using these State estimates, the Social Security Administration prepares a consolidated budget for the entire country sufficient for the "proper and efficient administration" of the programs. After review and possible amendment by the Bureau of the Budget acting on behalf of the President, the consolidated budget is submitted to the Congress. The amount appropriated by Congress is distributed among the States in accordance with State factors determined by the Social Security Administration.

The Council believes that it is important for the Federal Government to continue its responsibility for assuring to each State enough funds to administer the program in accord with at least minimum Federal standards, and therefore recommends that the Federal Government continue to bear financial responsibility for paying the costs of proper and efficient administration of the program. We believe, however, that it is important to provide an additional source of funds for the administration of unemployment insurance which would make it possible for certain States to pioneer in administration and do more than the minimum which the Federal Government is willing to approve as necessary for all States. This purpose can be accomplished by providing that some funds which could be used for administration be automatically assigned to the States.

At present, the 0.3 percent of covered pay roll which the Federal Government derives from the Federal unemployment tax goes into the Treasury of the United States without earmarking. The hearings and committee reports at the time the tax was imposed, however, clearly indicate that this revenue was intended to finance the administrative costs of the program. Actually the income from this tax has greatly exceeded administrative costs over the period since it was first imposed.<sup>16</sup> The Council believes that this Federal "profit" is unjustified and that the proceeds of the Federal tax should be earmarked for the use of the employment security programs. One-half of any surplus over expenses incurred in the collection of the tax and the administration of unemployment insurance and the employment service should be appropriated to the Federal loan fund (recommendation 10, p. 168) and one-half of the surplus should be assigned to the States—each State getting the proportion that taxable wages in that State bear to all taxable wages in the United States. The amounts so credited could be used on the State's initiative for either administration or benefits. The Council believes that the right to use excess funds for administration should be limited to 3 years after receipt of the funds. Thereafter, any excess funds which had not been used for administration would be available only for the payment of benefits. The Council believes further that the administrative standards in the

<sup>16</sup> Grants for administration under title III of the Social Security Act and the costs of collecting the tax have fallen some \$970,000,000 short of the amount collected by the Federal Government. When the total expenses of the employment service as well as administrative costs of unemployment compensation are subtracted from the Federal income from this tax, the balance is somewhat less than half a billion dollars.

Social Security Act should be applicable to the expenditure of the surplus funds as well as to expenditures of the funds originally appropriated.

The employment-security programs are particularly sensitive to changes in economic conditions, making it difficult to budget adequately for administration. At present it is frequently necessary to appeal to Congress for deficiency appropriations and for the Federal Government to deny much-needed funds to the States until such appropriations are available. To correct this situation, a contingency item should be added to the regular congressional appropriations for the administration of the employment-security programs.

The Council wishes to emphasize that the 0.3 percent of taxable wages may not always be the exact amount which should be earmarked for administration; it is hoped that States will continue to find means of cutting costs. Likewise, to the extent that broadened coverage includes groups presenting administrative problems, costs may rise. Similarly a radical change in the employment situation would greatly increase administrative costs. A period of experimentation will determine whether the amount is too great or too small. Subsequent changes can then be made.

#### 14. Clarification of Federal Interest in the Proper Payment of Claims

*The Social Security Act should be amended to clarify the interest of the Federal Government not only in the full payment of benefits when due, but also in the prevention of improper payments*

The Social Security Act now directs the Federal agency to withhold the payment of administrative expenses unless a State law provides for methods of administration such as "to insure full payment of unemployment compensation when due."<sup>17</sup> Furthermore, the Administrator is authorized to halt payments for administrative expenses to any State when he finds that, in the administration of the law, there is "a denial, in a substantial number of cases, of unemployment compensation to individuals entitled thereto under such law."<sup>18</sup> The present Federal law thus clearly holds the Federal agency responsible for seeing that State agencies pay valid claims, promptly and in full.

The Social Security Act is not equally specific about Federal responsibility for assuring that the State laws provide for administration reasonably calculated to prevent payment of invalid claims. While the Federal agency has taken some responsibility in this area, its statutory authority in relation to payments on invalid claims has been less clear than in relation to the failure to make payments on valid claims.<sup>19</sup>

The Council believes that the integrity of the system would be gravely threatened by payment of benefits which are not due as well as by failure to make payments when due. An amendment should therefore make it clear that the Congress intends the Federal agency to refuse to certify grants for administrative costs when the evidence of inadequate administrative methods is either the denial of valid claims or the payment of invalid claims.

<sup>17</sup> Sec. 303 (a).

<sup>18</sup> Sec. 303 (b).

<sup>19</sup> Both the Social Security Administration and the States, however, have for some time been concerned with the problem of erroneous and fraudulent claims; appendix IV-B deals with this subject at greater length.

One way of clarifying this intent would be to add to section 303 (a) of the Social Security Act the phrase "but only to individuals entitled thereto." It would then read in part:

The Administrator shall make no certification for payments to any State unless he finds that the law of such State \* \* \* includes provision for such methods of administration \* \* \* as are \* \* \* reasonably calculated to insure full payment of unemployment compensation when due, *but only to individuals entitled thereto.*

Although we believe that the total number of cases of deliberate fraud is relatively small, despite the widespread public attention given to such cases, all reasonable effort should, of course, be made to prevent fraud and eliminate all types of unwarranted payments. This result will be achieved mainly by improving methods in determining eligibility. The determination of eligibility in unemployment insurance is extremely difficult. The facts needed are hard to obtain and the questions to be decided are susceptible of widely differing interpretations. To determine what constitutes "suitable employment," "good cause for not accepting suitable employment," "availability for work," "a voluntary quit," for example, requires first the formulation of general interpretations of the statutory terms and then the application of the interpretations to a specific set of facts gathered largely through the interviewing process.

Anything short of carefully conducted interviews by specially trained and selected personnel of high caliber inevitably results in a large volume of unwarranted payments, some of them on deliberately fraudulent claims, and others merely erroneous. Even more important, badly conducted interviews result in disqualifying many claimants who are really entitled to payments. Both the failure to make proper payments when due and the payment of unwarranted benefits result mainly from the claimstaker's lack of skill or his or the worker's or employer's failure to understand the provisions of the law. Improper payments can be eliminated only by improvement of educational and training programs for employed personnel and by an increase in the amount and quality of information made available to the public.

The Council recognizes that under the present program administration of the unemployment insurance programs is primarily a State responsibility and that the quality of administration will necessarily depend in large part on the caliber of the personnel the State selects to do the job. Nevertheless, the Federal Government is concerned with the quality of administration both in determining whether a State is entitled to administrative funds through conformity with certain basic administrative standards and in approving funds for proper and efficient administration. In our opinion, improved administration is of major importance in the development of the unemployment insurance program. A major reason for our recommendation for changes in the provisions for financing administrative costs (recommendation 13, p. 172) is to insure the availability of more funds for this purpose.

## RECOMMENDATION ON DISQUALIFICATIONS

### 15. Standards for Disqualifications

*A Federal standard on disqualifications should be adopted prohibiting the States from (1) reducing or canceling benefit rights as the*

*result of disqualification except for fraud or misrepresentation; (2) disqualifying those who are discharged because of inability to do the work; and (3) postponing benefits for more than 6 weeks as the result of a disqualification except for fraud or misrepresentation.*<sup>20</sup>

Under most State laws workers are "eligible" for benefits only as long as they continue to be able to work and available for work.<sup>21</sup> In addition, they may be "disqualified" for benefits even though they are able to work and available for work and meet all other eligibility requirements. These disqualifications are imposed for three major reasons: "Voluntary leaving," the "refusal of suitable work," and "misconduct connected with the work." (See table 9, appendix E, for summary of disqualification provisions in State laws.)

In the Council's opinion, reasonable disqualification provisions should be maintained and strictly enforced to prevent payments to those who are unemployed through their own voluntary act or because they have failed to make a reasonable effort to hold a job. In some States, however, disqualification provisions have been introduced which deny benefits to individuals who are genuinely unemployed through no fault of their own and are ready, willing, and able to accept suitable work. In other States, unreasonable penalties have been attached to the disqualifying acts.

1. *Provisions which cancel or reduce benefit rights.*—In 22 States benefit rights are now canceled or reduced for some cause other than fraud or misrepresentation. Such reduction or cancellation means that those who are disqualified not only are denied benefits for unemployment immediately resulting from the voluntary quit, refusal of suitable work, or discharge for misconduct, but also lose accumulated benefit rights which would otherwise be available to them if they are subsequently employed and suffer a second spell of unemployment. The Council condemns the intent and effect of these provisions. Such cancellation and reduction deny benefits in periods of unemployment for which the propriety of compensation is not open to question. The Council recommends the establishment of a Federal standard to prohibit the cancellation or reduction of benefit rights except for fraud or misrepresentation.

2. *Interpretations of "misconduct" tending toward making discharge for inability to do the work a basis for a finding of misconduct.*—The concept of involuntary unemployment should undoubtedly exclude unemployment resulting from discharge, if the worker has made no real attempt to hold the job and if the reason for his discharge is insubordination, consistent refusal to follow shop rules, or other types of gross misconduct. Failure to perform adequately in a job, however, is most commonly due to inadequate training, poor placement, and other inadequacies attributable to both management and worker. To deny benefits because a worker cannot measure up to criteria established by the employer under conditions primarily under

<sup>20</sup> Three members of the Council are of the opinion that there should be no Federal standards relating to disqualifications beyond those now in the act. They believe the underlying principle of the present State-Federal system is that wide discretion be left to the individual States and that by compelling all States to accept the proposed standards, this principle would be violated and a considerable number of States would be required to change their laws. They also point out that there is a wide divergence of opinion regarding the merits of disqualification provisions in State laws, and that some provisions have been introduced in an effort to reduce improper payments. They maintain that if some States have gone too far, public opinion within the State will bring about a change.

<sup>21</sup> In five States a worker who was able to work at the time of filing a claim but became ill while still unemployed may nevertheless continue to receive benefits.

the employer's control is, in the Council's opinion, to deny benefits to many whose unemployment can in no sense be considered as voluntarily incurred.

3. *Excessive postponement of benefits or denial of benefits during the entire spell of unemployment because of a disqualification.*—Some States (11 with respect to voluntary leaving, 6 for misconduct, and 12 for refusal of suitable work) withhold benefits for any period within the spell of unemployment following such action. Certainly a worker should not receive benefits if his actions are not consistent with a genuine desire for work; and voluntary leaving, refusal of suitable employment, and other causes of disqualification raise a presumption that he does not desire work. This presumption, however, should not apply to the whole spell of unemployment regardless of its length. The basic question is whether the entire spell of unemployment following a voluntary quit, refusal of work, or misconduct can reasonably be considered voluntary unemployment or whether, after a limited period, if the worker remains able to work and available for work, the continued unemployment is not due to lack of suitable work. The Council believes that 6 weeks is probably the maximum period during which it is reasonable to presume that the original disqualifying act continues to be the main cause of unemployment.

A Federal standard such as we propose would in no way prevent States from imposing a shorter period of disqualification, either in all cases or on a basis which would vary with the particular disqualification. A new "refusal of suitable employment," of course, could result in postponement of benefits for an additional 6 weeks and States would be allowed to postpone benefits for longer periods than 6 weeks for fraud or misrepresentation.

Opinion within the Council is divided on whether it would be desirable to propose an additional Federal standard prohibiting State laws from disqualifying persons because their unemployment is not "attributable to the employer" or "connected with the work." There are now 16 State laws which have such provisions. They rule out personal reasons as good cause for leaving a job. All members of the Council agree that the payment of benefits to persons who leave jobs for personal reasons should not be reflected in the employer's experience rating and most members of the Council favor the practice that several States now follow—paying benefits in such cases but not counting the benefits for experience-rating purposes.

The division within the Council is related to the question of how far the Federal Government should go in requiring the States to compensate for unemployment attributable to personal reasons rather than to the question whether it is desirable for the States on their own initiative to compensate for such unemployment. Some members feel that the States should be required to compensate for unemployment arising in such instances as when a worker moves to a new locality for the sake of his own health or that of his family, or he leaves one job to accept an offer of work which is later withdrawn. Another example of unemployment attributable to personal reasons which is not compensated in some States is that which results when a worker who recovers from an illness finds that his old job has been filled and that he must seek another; the unemployment under these rulings is not com-

pensated because it is not "attributable to the employer." Other members of the Council feel that the decision whether unemployment resulting from such causes should be compensated should be left entirely to the States.

## RECOMMENDATION ON PLANS SUPPLEMENTARY TO UNEMPLOYMENT INSURANCE

### 16. Study of Supplementary Plans

*The Congress should direct the Federal Security Agency to study in detail the comparative merits in times of severe unemployment of—(a) unemployment assistance, (b) extended unemployment-insurance benefits, (c) work relief, (d) other income-maintenance devices for the unemployed, including public works. This study should be conducted in consultation with the Social Security Administration's Advisory Council on Employment Security, the Council of Economic Advisers, and the State employment security agencies, and should make specific proposals for Federal measures to provide economic security for workers who do not have private or public employment during a depression and who are not adequately protected by unemployment insurance*

The Council recognizes that the burden of unemployment in a severe depression cannot be met in any one way. Neither unemployment insurance nor any other single method will be sufficient to do the whole job. A complete system of social security would provide for various types of plans to supplement unemployment insurance in times of large-scale unemployment.

The Council intended to make recommendations concerning the merits and shortcomings of the various possible plans and, in submitting recommendations on public assistance, said: "In its report to be submitted on unemployment insurance, the Council plans to consider the problem of the responsibility of the Federal Government for the income maintenance of workers in time of business depression."<sup>22</sup> We regret that we have been unable to make the thorough study of alternative lines of action on which to base a policy decision in this area. We believe, however, that it is important that the Federal Security Agency study alternative methods of providing income security for workers who do not have private or public employment during a depression and who are not adequately protected by unemployment insurance and that preliminary plans be completed for putting the best methods into effect. We therefore recommend that the Congress direct the Federal Security Agency to make such a study in consultation with its Advisory Council on Employment Security, the Council of Economic Advisers, and the State employment security agencies.

The State-Federal system of unemployment insurance should pay benefits of sufficient duration to permit most covered workers in normal times to find suitable employment before their benefit rights are exhausted. Furthermore, the Council has recommended that the State-Federal public assistance program be strengthened to meet more adequately the needs of unemployed workers ineligible for in-

<sup>22</sup> See p. 103.

insurance benefits or with inadequate insurance rights.<sup>23</sup> These dual provisions for the unemployed through the State-Federal programs would suffice, the Council believes, unless the country is again plunged into a period of severe and prolonged economic distress. In that event, additional Federal action would clearly be needed for the relief of the unemployed. A depression has an uneven impact upon different cities and regions and many States and localities are not capable of meeting the great increase in expenditures called for by mass unemployment. In such a period only the Federal Government has sufficient credit and sufficiently broad eventual tax resources to meet the full need.

The Council does not anticipate a return to the economic stagnation of the 1930's, but believes that it is prudent to prepare for a heavy volume of unemployment even while steps are being taken to prevent its recurrence. The Council cites without specific recommendation various types of possible Federal action. We wish to emphasize that whatever methods are used the integrity of the insurance system should be maintained and separate financing should be provided for the supplementary plans.

(a) *Unemployment assistance.*—A special program of unemployment assistance might be used for persons who do not come under the unemployment insurance program either because of its failure to cover all types of work or because many members of the covered labor force are unable to meet the eligibility requirements in times of depression. Depressions greatly increase the number of persons who seek work for the first time to supplement the family income, and the number of formerly self-employed persons looking for jobs also rises. Moreover, as the depression deepens, the number of wage earners who lack recent earnings in covered employment increases, hence the insurance system bears a smaller and smaller proportion of the load of unemployment.

A State-Federal unemployment assistance plan might be established with the same scale of Federal contributions as those recommended in the Council's report on public assistance for old-age assistance, aid to the blind, and aid to dependent children (three-fourths of the first \$20 plus one-half up to \$50 for the first two in a family plus \$15 for each additional person). If the depression were prolonged, some States might be unable to meet their share of unemployment assistance payments without additional Federal help. The Federal Government, as in the 1930's, might take over almost all costs, or it might lend the States their share.

(b) *Extended unemployment benefits.*—Another possibility would be to permit extension of unemployment benefits at the same rate and to the same persons for an additional 13 or 26 weeks. If extended benefits are granted, the beneficiary might be required to take a training course or move to an area offering better employment opportunities. A needs test, however, would not be applied. A separate plan for financing extended benefits should be provided either on a joint State-Federal basis or by the Federal Government alone. Otherwise, extended unemployment benefits would undermine the unemployment insurance system.

(c) *Work-relief program.*—In the 1930's Congress spent billions of dollars on a series of work-relief projects. Debates over the advan-

<sup>23</sup> Recommendation 2 in pt. III, p. 108, provides for Federal grants for "general assistance."

tages and disadvantages of work versus cash relief are still raging long after the demise of NYA, CCC, and WPA. Advocates of work relief may admit the folly of some projects, but they point to thousands of successful ones which have added significant value to the American economy. They also argue that many relief workers received training on the job and that work habits were maintained better than if cash relief had been the only method used. The advocates of cash relief cite its great simplicity and economy, and argue that most of the best work-relief projects competed with private industry or regular Government work and that work relief in many cases fostered bad work habits rather than maintained good ones.

(d) *Other income—maintenance devices for the unemployed, including public works.*—Quite apart from unemployment insurance, unemployment assistance, extended unemployment insurance, and work relief, the Federal Government might, in times of serious depression, increase its spending on essential public works. Such action would stimulate employment primarily in the construction industries, secondarily in industries supplying the construction industry, and indirectly in the industries whose products are consumed by workers employed on the projects and in the supplying industries. On the basis of past experience, however, it is clear that public works alone are insufficient for a large number of the needy unemployed. Although in other recessions large numbers of construction workers have been unemployed, the secondary and subsequent effects of increased public works were not enough to give employment to many other groups who needed jobs. Although the Council recognizes the advantages of planning public works in good times and expanding them in periods of slack employment, it considers public works as an incomplete solution of the problem of widespread depression unemployment among persons ineligible for unemployment insurance benefits.

Various combinations of the methods discussed above might be used. Other plans have also been suggested such as self-help groups, share-the-work plans, and guaranteed employment.

Throughout the country, both in business and labor groups, there is a widespread conviction that serious cyclical recessions can and should be minimized. Many general proposals have been made to promote full employment, and Congress has established a Council of Economic Advisers to deal specifically with this problem. If these attempts are successful, supplementary plans will not be needed, but as a safeguard against hasty and ill-conceived schemes, it will be well to have a sound plan ready if, despite all efforts, the country is again faced with the problem of large-scale unemployment.

## TEMPORARY DISABILITY INSURANCE

The Council in its second report to the Senate Committee on Finance presented recommendations for a program that would afford protection to workers against the loss of wages due to permanent and total disability.<sup>24</sup> Under these recommendations, benefits would be provided only to workers who have been disabled for a period of at least 6 months when it appears likely that the disablements will be of long-continued and indefinite duration. Because time was lacking for a comprehensive study of the various methods that have been proposed to afford protection to workers who are unemployed because of temporary disability, the Council refrains from making any recommendations covering this area. The Council, however, recognizes that the loss of income from temporary disability is a major economic hazard to which all wage earners are exposed. In lieu of recommendations, a summary statement on the need for providing protection against wage loss due to temporary disability, the scope of existing programs, and some of the methods that have been suggested by various groups to afford workers such protection is presented below.

On the average day, illness prevents about 2 to 2½ million persons recently in the labor force from working or seeking work. In a year wages amounting to 5 to 6 billion dollars are lost because of disabilities lasting up to 6 months. The economic hardship caused by disability may be an even more serious hazard to workers than is wage loss, because illness entails medical expenses as well as the loss of income. Unlike the situation in other major industrialized countries, however, compulsory protection against wage loss due to temporary incapacity in this country is largely confined to work-connected accidents and diseases in industry and commerce which are covered by workmen's compensation programs. Only three States (Rhode Island, California, and New Jersey) have provided for the payment of benefits for temporary disability to workers covered by their unemployment-insurance laws. In addition, the railroad unemployment-insurance law has been extended to provide cash sickness benefits to workers covered by that law.

In recent years, voluntary health and welfare plans provided under collective-bargaining agreements have expanded materially. While such plans may provide excellent protection against the loss of income from temporary illness or other disablements for the groups economically powerful enough to obtain such protection, large groups of workers continue to remain unprotected under voluntary health and welfare plans. A study made in New York State indicated that only about 30 percent of the workers now covered by unemployment insurance have some protection against wage loss due to disability under group health and accident policies or formally established employer plans. For the country as a whole, an estimated 20,000,000 workers

<sup>24</sup> See pp. 69-93.

who are covered by State unemployment-compensation programs have no protection under formally established voluntary sickness-benefit plans. The extension of such protection to all employees in industry and commerce is unlikely because individual premium rates under commercial group insurance policies make coverage expensive for industries in which a relatively high incidence of disability may be expected. For instance, when women and nonwhite employees constitute 51 to 60 percent of the total number of eligible employees, rates for manual workers are 62.5 percent higher than the minimum—and increase proportionately to 112 percent higher when all eligible employees are women or nonwhite. Furthermore, group contracts are not suitable for small establishments; the smaller the number of employees, the greater the probabilities that the distribution by age and sex, as well as health of employees, will differ from the norms for establishments with a large number of employees. It is not uncommon for underwriters of group health and accident insurance to refuse to insure groups of less than 50 employees, while State insurance laws frequently prohibit issuance of group policies to groups of less than 25. Moreover, under any voluntary plan of affording protection to workers against the loss of wages, the employers who pay the lowest wages and whose employees consequently are in greatest need of protection would be the least likely to participate in such a plan.

The New Jersey State Commission on Postwar Economic Welfare, after considering the need for temporary disability insurance and the possibilities for coverage under voluntary plans, came to the following conclusion:

Popular opinion also overwhelmingly favors the extension of some form of social security legislation to protect against the hazards of illness. Particularly in the lower income levels, where the frequency of nonoccupational illness seems to be greatest, people suffer most severely from the economic effects of wage loss. Since it is an accepted public policy to protect the individual against wage loss caused by involuntary unemployment, it seems desirable to fill the gap in this protection by meeting the hazards of inability to work caused by sickness. The public interest in social and economic security and stability is as much served in the one case as in the other.

While the progress made in supplying protection against wage loss caused by illness through voluntary programs adopted by employers has been great, the need for the extension of such protection is so great as to warrant the establishment of some form of uniform minimum standard coverage. Given sufficient time, the voluntary program might very well be extended greatly, but there would always remain a significant number of people for whom either no provision has been made or for whom inadequate provision has been made. The establishment of a minimum standard and its enforcement is essentially a function which must be performed by government, in whatever manner benefits may be provided. It remains to determine the best method by which such minimum benefits may be provided and financed.<sup>25</sup>

The four existing laws providing insurance against temporary disability—the Rhode Island, California, and New Jersey State laws, and the Federal law for railroad workers—are very closely allied with the respective unemployment insurance laws in both substantive provisions and administrative arrangements. The same groups of workers are covered, the same type of formula determines the benefits payable, the same measure of attachment to the labor force is used, and except in the New Jersey plan for disability during employment, the same “base periods” and “benefit years” are used for temporary dis-

<sup>25</sup> Fourth Report of New Jersey State Commission on Postwar Economic Welfare, pp. 9-10.

ability and for unemployment insurance. While the New Jersey plan has no "benefit year," minimum and maximum benefits in any 12-month period are determined on the same basis as in unemployment insurance. All four statutes are administered by the unemployment insurance agencies, and thus use the same administrative machinery for collecting contributions, for maintaining wage records, and for staff services for both programs. Obviously, because disability rather than availability for work must be demonstrated by the claimant, the claims procedures are markedly different.

Benefits have been payable in Rhode Island since April 1, 1943, in California since December 1, 1946, and under the railroad system since July 1, 1947. In New Jersey, benefit payments will begin on January 1, 1949.

The most distinctive difference among the four programs is the provision in the California and New Jersey plans for a State-supervised system of private voluntary plans which may be substituted for the State-operated plan. (See appendix IV-D, table I, for comparison of the four temporary disability laws.) The voluntary plans, however, must fulfill certain requirements specified in the respective statutes. The California law requires that a private plan must afford more favorable rights to the employees it covers than are afforded by the State plan, at no greater cost to the employees; the plan must be available to all employees, must be accepted by a majority, and must not result in a substantial selection of risks adverse to the State fund. The New Jersey requirements differ in that the rights afforded under the private plan must at least equal those under the State plan, at no greater cost to the employees; if a majority of the workers in a plant accept a private plan, all the workers of that plant must be covered under it rather than under the State plan; and there is no other provision against adverse selection. Both laws contain other requirements designed to assure that the benefits promised by the private plans will actually be paid.

Voluntary private plans may be either self-insured by the employer or carried by a properly qualified insurance company. If a plan is approved as meeting the requirements of the State law, the employees covered by it receive their disability benefits under the voluntary plan and are exempted from paying contributions to the State fund. On June 30, 1948, there were over 10,000 employers with approved voluntary private plans in effect in California (5 percent of the covered employers), which covered about 765,000 workers or 32 percent of the total number covered by the unemployment insurance and disability law.

Benefits under the State-operated systems in California and Rhode Island (which has no provision for the substitution of private voluntary plans for the State system) are financed exclusively by employee contributions of 1 percent of wages up to \$3,000. In New Jersey, benefits under the State-operated system are financed by an employee contribution of 0.75 percent and an employer contribution of 0.25 percent. The current contribution rate for the railroad temporary disability insurance system and unemployment insurance is 0.5 percent levied on employers. In all four laws, the weekly benefit amount is determined according to a schedule and related to previous wages; in Rhode Island the amount ranges from \$6.75 to \$18; in California from \$10 to \$25; in New Jersey from \$9 to \$22; and under

the railroad system the amount for a 2-week period ranges from \$17.50 to \$50. The maximum duration of benefits ranges from 3 to 20 weeks in Rhode Island, from 10 to 26 weeks in California, and from 10 to 26 weeks in New Jersey, depending on the amount of base-period wages. The railroad system provides a uniform potential duration of 26 weeks.

The New Jersey law actually provides three systems, one for workers unemployed when they get sick, one for those who are employed and not covered by private plans, and a third for those covered by private plans. For those employed at the time the disability begins, the weekly benefit amount is computed for the period of disability, and the maximum and minimum benefits mentioned above apply to any 12-month period. The individual is considered disabled when he is unable to perform the duties of his current job. The worker who is unemployed when he becomes disabled, however, must be unable to perform any work for remuneration if he is to be eligible for disability benefits. Moreover, he must have established a benefit year by a claim for unemployment benefits and must have served the 1-week unemployment insurance waiting period.

Disability due to pregnancy is treated quite differently under the four laws. Rhode Island considers pregnancy a disability whenever a woman is not working during pregnancy; maximum benefits for any one pregnancy, however, are limited to 15 weeks, except for unusual complications, and may be less, depending upon the amount of base-period wages. Under the New Jersey law, on the other hand, no payments are made for periods of disability due to pregnancy. California will pay for periods of disability lasting more than 4 weeks after the termination of pregnancy. The railroad act provides separate maternity benefits which are in addition to the ordinary duration of benefits; the maternity benefits are paid for 16 weeks, beginning 8 weeks prior to the anticipated date of confinement.

Temporary disability insurance is intended to protect against wage loss due to nonoccupational disability and is not a replacement for workmen's compensation, which continues to bear the costs of work-connected injury and disease. The existing laws provide for varying methods of coordination between the two programs. Rhode Island is the most liberal, permitting the payment of both types of benefits up to a weekly total of 90 percent of the weekly wage rate before the disability.

In June 1948, about 5.5 million workers (of the 34.3 million workers covered by unemployment insurance laws) were covered under the 4 existing laws for temporary disability insurance, 4.2 million of them under the 3 laws which had been paying benefits for at least 12 months on June 30, 1948.

During the year ended June 30, 1948, more than 50.3 million dollars was paid in temporary disability insurance benefits, with 50,700 disabled workers receiving benefits in an average week. Of the total benefit expenditures, 26.6 million dollars was paid to railroad workers—0.56 percent of taxable railroad wages. The California State plan paid out 19.4 million dollars—0.41 percent of the wages taxed under the State plan; an additional 56,000 spells of disability were compensated by approved private plans. Rhode Island benefits were 4.3 million dollars—0.78 percent of taxable wages. (See appendix

IV-D, table J, for summary of operations of California, Rhode Island, and railroad programs.)

During the year, there were three railroad sickness beneficiaries for every four unemployment insurance beneficiaries in the same period. In Rhode Island, there were two temporary disability insurance beneficiaries in an average week for each five unemployment insurance beneficiaries, while under the California State plan, disability accounted for only one beneficiary in an average week for every seven beneficiaries for unemployment insurance. These variations can be explained in terms of variations in the unemployment rates and in the characteristics of the covered groups, as well as differences in statutory provisions. Unemployment has been very low in the railroad industry during the past few years, while the ratios of insured unemployment to covered workers in California and Rhode Island have been among the highest in the country. Moreover, the average age of railroad workers is much higher than the average age of workers covered by a State law. The high proportion of women in the Rhode Island covered group, combined with the provision for benefits in cases of pregnancy, increased the number of Rhode Island beneficiaries.

Various methods have been suggested by interested groups to provide temporary disability insurance for workers in all States. These proposals differ on such points as whether the program should be established by State legislation, Federal legislation, or a combination of both. Further, the various proposals differ in respect to the administrative agency that would be responsible for the program. Among these proposals are those that would (1) integrate temporary disability insurance and unemployment insurance, (2) integrate temporary disability insurance and permanent and total disability insurance with old-age and survivors insurance, (3) provide only for State-supervised private plans, and (4) integrate temporary disability insurance with medical care insurance.

The proposal to integrate temporary-disability insurance with unemployment insurance has had considerable acceptance. As has been noted above, all four of the existing temporary-disability programs are closely linked with the unemployment-insurance programs. The Congress in 1946 enacted legislation to permit employee contributions collected by the States for unemployment-insurance purposes to be used to support State temporary-disability-insurance systems. Most of the bills for temporary-disability insurance that have been introduced in State legislatures would provide for the integration of the two programs.

The proponents of this method of affording protection to workers point to the economy to be derived from using the same administrative machinery and similar substantive provisions for both programs. In general, these proponents also recognize that a temporary-disability insurance program poses some problems that are not common to unemployment insurance and would therefore require certain special provisions, procedures, and staff to meet these problems. It has been argued that, for both programs, coverage could be afforded the same workers; the same covered wages and pay rolls could be used as a basis for contributions; and even if the benefit formula were somewhat different for temporary-disability insurance, the same wage credits could serve as a basis for benefits under both programs.

Although proponents for integration of these two programs may agree on the desirability of such action, sharp differences of opinion are expressed among them on the degree of responsibility for the temporary-disability system that should be vested in the State unemployment-insurance agency. Some advocate an exclusive State system, while others advocate a State-operated system, plus substitute State-supervised private plans. As has been noted above, the first type of system has been adopted by Rhode Island, and the second by California and New Jersey. Those who advocate an exclusively State-operated system argue that pooling all risks on a State-wide basis results in a higher level of benefits (or lower contributions) than if the risks were shared with private plans, since the latter would not cover poor risks. Further, it is claimed that, when any private plan proves unprofitable, the group covered by such a plan is eventually turned over to the State-operated system. The proponents of an exclusively State-operated system also point out that a State agency, unlike insurance companies engaged in the business of insuring workers under a private plan, earns no profit and incurs no sales cost; so that, if the State system is permitted to insure all eligible workers, the proportion of contributions available for benefit payments is larger than under any other system. Recognition of private plans, it is argued, will also add to administrative problems because of the need for review and supervision of these plans and the need to assure continuity of coverage and prevention of duplicate payments to workers moving from one type of plan to another.

Those who favor a State-operated system plus substitute State-supervised private plans emphasize that all eligible workers acquire protection, either under the State-operated program or under substitute private plans approved by the State supervisory agency. They claim that this type of system, whereby the employees and employer may choose between the public or private plans, provides a high degree of flexibility and avoids freezing benefits at a statutory minimum level. Workers who are now covered by generous private plans could retain that coverage if the employer agreed and the State agency approved, thereby avoiding the need to transfer many workers to a system paying lower benefits. Similarly, private plans with provisions more liberal than those offered by the State law could be adopted if employers and employees desired and were able to pay for better protection, and employers would have a more direct interest in the plan. The advocates of this type of system also claim that competition between a State-operated plan and private plans stimulates more economical and efficient administration of both plans.

Proponents for integration of temporary-disability insurance and unemployment insurance disagree on the role of the Federal Government in such a program. Some advocate complete federalization of both unemployment and temporary-disability insurance; others say that the program should be exclusively a State responsibility; while many other types of action advocated fall between these two extremes.

Those who favor Federal action argue that the Federal Government has as vital an interest in protecting the workers of the country against the loss of income from disability as it has in seeing that they are covered by unemployment insurance. They argue that, if workers in all States are to get this additional protection within the foreseeable

future, Federal action will be needed; and they cite the delay of 37 years in obtaining workmen's compensation in all States as compared with the 2-year period required to obtain unemployment insurance on a Nation-wide basis.

A number of the alternatives for Federal action short of complete federalization are listed below:

1. The Federal Government might pay the administrative expenses of State temporary-disability-insurance systems in the same manner as it now pays such expenses for unemployment insurance.

2. The Federal Government might go further and permit the use of State accounts in the unemployment trust fund to finance State systems of temporary-disability insurance under adequate safeguards for the solvency of the funds.

3. The Federal Government might make the establishment of a disability program a condition for the continued receipt of the tax offset under the present tax on employers for unemployment insurance.

4. The Federal Government might extend the Federal-State device used in unemployment insurance by levying a Federal tax for temporary-disability insurance.

Those who advocate the integration of temporary-disability and unemployment insurance under State laws, without any Federal legislative action, claim that State-Federal programs result in at least some control over the State agencies administering the programs; that such control sometimes makes it impossible for a particular State to use the best methods of meeting problems that are peculiar to the State; and that even limited Federal responsibility sometimes stifles State initiative and experimentation, which are especially important in developing sound programs in a relatively new area of the social-security field.

The proposal to integrate a temporary disability program and a permanent-and-total-disability program with old-age and survivors insurance has received considerable attention in recent months. The proponents of this plan cite the economy to be obtained from using the Nation-wide old-age and survivors insurance administrative machinery for payment of benefits and collection of contributions for a disability program, and the convenience to the public in having one field office for the filing of claims and the handling of wage questions for the three programs. They claim that only under a Federal program would workers have uniform protection against the loss of wages from illness regardless of State of residence or employment. These proponents also contend that, since temporary-disability insurance and permanent-and-total-disability insurance both need to establish disablement, the special staff and special procedures required for determining medical disability in one program could be utilized for the other. If the two disability programs were not integrated, much duplication of staff and procedures would be necessary. Furthermore, these proponents claim that, because many of the persons who will become eligible for permanent-and-total-disability benefits will first be eligible for temporary-disability benefits, a single administrative agency would be able to emphasize rehabilitation service for disabled persons at the earliest possible time instead of delaying such service until a claimant has become a beneficiary under the permanent-and-total-disability program. Similarly, it is claimed that integration of

the two programs will eliminate many of the gaps in protection against the loss of wages from disability that would exist under two separate programs.

The plan to provide temporary-disability insurance by the exclusive use of State-supervised private plans has been advocated by those who recognize the need for protection from wage loss during temporary disability but who believe such protection can best be provided by the purchase of group insurance or by self-insurance by employers. Under this plan, there would be no State-operated program; but, instead, private plans would be required under compulsory State legislation which would make it necessary for employers to provide a minimum level of protection to employees.

Many of the arguments in favor of this plan are similar to those that are advanced for permitting private plans to be substituted for a State-operated system. The proponents of the exclusively private-plan system argue that such a system would provide a high degree of flexibility and avoid freezing benefits at a statutory level; would permit the continuation of existing employer plans or the adoption of new plans if employers and employees desired and were able to pay for better protection; and that the employers would have a more direct interest in the system.

The advocates of this plan usually admit that some difficulties may arise in assuring protection to employees of some employers who may not be readily able to obtain insurance or to meet all the State requirements. They claim, however, that a solution to such difficulties can be found; and they cite the operation of workmen's compensation in jurisdictions that have exclusively private plans for that program as a precedent for the workability of a similar plan for a temporary disability program.

The plan to integrate temporary-disability insurance with medical-care insurance has been proposed by some of the advocates of the latter program. Under this plan, cash benefits would be paid for loss of wages due to temporary disability; and direct payments would be made to doctors, hospitals, and so forth, furnishing medical care to eligible persons. Although the two programs would be administered by one agency and persons receiving cash benefits would receive medical care, the latter service would also be available to others covered by the medical-care provisions.

Those who favor this plan cite the economy to be obtained by using one wage-record system and one administrative organization to serve both programs. They argue that, because the medical staff needed for one program would also be available for the other, such integration would permit better utilization of the time of the medical profession than would any other system. Furthermore, they claim that integration of the two programs would make rehabilitation services available without delay to those who could benefit from such services.