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Federal–State Relations in Labor Exchange Policy

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In 1933 the United States Employment Service was created—a cooperative State and Federal enterprise. . . . The Federal–State cooperation has been splendid.

Franklin D. Roosevelt
September 6, 1936

This chapter will describe noteworthy policy issues over the past decade that affected federal–state relations in the delivery of labor exchange services funded under the Wagner-Peyser Act of 1933. We will explain how the intergovernmental structure of the public employment service (ES) established under the Wagner-Peyser Act faced serious challenges during the 1990s and ultimately was strengthened. This was an era aptly described by Nathan and Gais (2000) as Second Order Devolution—a type of federalism that extols the merits of local authority and privatization of government services. While we will focus primarily on labor exchange policy of the 1990s, we also will summarize labor exchange policies from President Roosevelt’s New Deal of the 1930s to President Reagan’s New Federalism of the 1980s, and speculate on President George W. Bush’s labor exchange policy.

The division of power between state and local control of workforce development programs is a pivotal issue of workforce federalism. Since the 1970s, a constant tension in workforce federalism has existed between state-administered labor exchange programs under the Wagner-Peyser Act and local-administered job training programs under the Comprehensive Employment and Training Act (CETA), the Job Training Partnership Act (JTPA), and the Workforce Investment Act (WIA).

The division of power between the Wagner-Peyser Act and job training laws during three eras of New Federalism is the subject of this chapter. Our policy lens will be focused primarily on federal policy making, leading up to and following the enactment of WIA in 1998.

We aim to demystify some of the seeming contradictions of workforce federalism during the era of New Democrat President Clinton that paradoxically strengthened state control of labor exchange policy while consolidating control of local workforce development services under the one-stop delivery system. We will examine the relationships between the federal government and state and local authorities during a decade marked by notable changes in national labor exchange policy.

LABOR EXCHANGE POLICY, FEDERALISM, AND THE APPORTIONMENT OF RESPONSIBILITY BETWEEN LEVELS OF GOVERNMENT

More than 30 years ago, Richard H. Leach (1970, p. 57) wrote that federalism was designed as a negative device to inhibit the use of power in the United States. The examination of federal–state relations in the administration of a public ES requires study of federalism’s competing ideologies during the last century: centralized government to meet the economic crisis of the Great Depression; and its counterassault, decentralized government dubbed *New Federalism*, which shifted power to state and local authorities in order to reduce big government and deficit spending.

The Federal–State Relationship

Under the U.S. Constitution, responsibility between the central (i.e., federal) government and subgovernments (i.e., states) is divided. A federal system limits the centralization of power by defining spheres of authority. The Tenth Amendment specifies that those “powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.” The term *local government* does not appear in the Constitution. Throughout the Republic’s history, the division of authority between

the federal government and the states has been contentious. Resulting from that tension has been a remarkable elasticity in the relationship between the levels of government. This relationship has sustained the people's general welfare and the capitalist market as authority has shifted back and forth to meet political and economic circumstances.

Cooperative Federalism and Labor Exchange Policy

By the early 20th century, nearly half the states and a small number of local governments created public employment offices to address Industrial Age dislocations resulting from economic downturns. In the 1930s, the mounting surge of unemployment incited a public demand for a national labor exchange policy. After an attempt to create a national ES system failed in 1931, two years later President Roosevelt signed into law the Wagner-Peyser Act.¹

Under the Rooseveltian New Deal, federal programs to aid states were implemented under a cooperative partnership. According to Vines (1976, p. 13), cooperative federalism refers to cooperative procedures to accomplish national policies established by the federal government; state and local governments receive federal funds called grants-in-aid² to administer public programs. During this period, direct federal intervention in state labor exchange policy helped shore up the U.S. economy through referral of unemployed workers by public employment offices to public works projects and establishment of a national ES system.

Under section 1 of the Wagner-Peyser Act, the U.S. Department of Labor (USDOL) was charged with 1) establishing a national system of public employment offices through a “confederation of permanent State employment services operating in cooperation with the Federal Government . . .” (Persons 1934), and 2) revitalizing the U.S. Employment Service (USES) by vesting responsibility for administration of the federal–state ES system under its aegis. In essence, the Wagner-Peyser Act set up a federal-directed, state-run system of public employment offices.

The Wagner-Peyser Act was enacted as a federal–state grants-in-aid³ program. States created ES agencies through legislation in order to receive federal grants for administration of local ES offices. Except during World War II, when state ES agencies were federalized to recruit

labor for industrial defense production, the ES has remained a federal–state cooperative program. Preceding enactment of the Wagner-Peyser Act and for the next three decades, policy debates on governance centered on whether the ES should be nationalized or whether the federal–state structure should be maintained (Haber and Kruger 1964, p. 67). The federal–state arrangement was chosen over an entirely federal scheme for several reasons, among them was that state control allowed greater flexibility and efficiency in the management of local ES offices (Persons 1934, p. 4).⁴

Coordination of the UI and ES programs

The Social Security Act of 1935 required the payment of unemployment benefits through public employment offices or other offices approved by the Social Security Board. The Social Security Board designated only state ES offices for the payment of benefits. With the passage in 1938 of UI laws in all states, the states charged their ES offices with administering the so-called *work test* whereby to qualify for benefits, UI claimants must be able to work, be available for suitable work, and must register for work (in most states).

According to some observers, this new responsibility brought a mixed windfall. While it increased the number and diversity of workers on file, over time it dulled the image of state ES offices through their relationship with UI and identification as “unemployment offices”—places that did not attract workers seeking first or better jobs. Despite this, and due in part to postwar prosperity, from 1946 to 1962, when the Manpower Development and Training Act (MDTA) was enacted, state ES agencies were viewed as employer oriented, as they were the sole

Labor Exchange Services

State ES agencies administer public labor exchange services without fee to job seekers or employers. Services for job seekers include assessment, together with interviewing, counseling, and testing; job search workshops; and job placement. Services for employers include job order taking, recruitment, screening, and referral of job seekers. Other services include matching job seekers and employers, administering work test requirements of state unemployment insurance (UI) laws, and producing and disseminating labor market information. Services under the Wagner-Peyser Act do not include skill training (section 7 of the Wagner-Peyser Act). Under Title I of WIA, adults and dislocated workers receive, without eligibility requirements, labor exchange services as core services from public and private service providers.

public employment agency designed to meet employers' production requirements. The federal role in state labor exchange policy was mostly passive, and no attempt was made to manipulate the labor market (Johnson 1973, pp. 13–15).

Creative Federalism and Labor Exchange Policy

By the late 1950s, America began to address the problems of poverty, race, and class. Early job training programs were contained in the Area Redevelopment Act of 1961 and the MDTA of 1962. State ES agencies were assigned responsibility to designate areas of high unemployment, analyze the local labor market to determine suitable occupations for training, and select and refer job seekers to training (Guttman 1990). In 1964, President Johnson declared an “unconditional war on poverty” and signed the Economic Opportunity Act (EOA) into law. To this end, the federal government instituted job training programs, called “manpower programs,” in local areas to aid disadvantaged workers.

Johnson referred to this period as *Creative Federalism* (Wright 1997, p. 583), in which grants established direct intergovernmental relations at substate levels, often bypassing state or local governments. According to Guttman (1990), an alternative workforce development structure was created under EOA, in part because of concern that state ES agencies might not be responsive to disadvantaged workers.⁵ Localities administered most manpower programs through grants-in-aid, and the job matching role of state ES agencies was deemphasized (Balducchi, Johnson, and Gritz 1997, p. 408). The ES was tradition-bound and slow in instituting active labor exchange policies to assist disadvantaged workers (Sundquist 1968, p. 68). State ES agencies played a subordinate role in the delivery of services to the disadvantaged.

New Federalism

During the 1970s, President Nixon reduced federal grants-in-aid and replaced them with block grants to state and local governments, with the intention of decentralizing welfare and workforce development programs that provided services to localities. This approach became known as *New Federalism*—a domestic policy framework that exalts state and local control over federal control. The evolution of New

Federalism as it applies to labor exchange policy is examined during three eras:

- 1) Permissive New Federalism (Vines 1976). Nixon's decentralized approach to workforce policies reduced grant-in-aid programs, instituted block grants, and established a federal–local training delivery structure under CETA.
- 2) Devolution New Federalism. Reagan's devolutionary approach to workforce policies revamped the federal–local training structure and labeled it JTPA, expanded state control of ES activities, joined state ES and local job training planning and budgeting cycles, and nearly abdicated federal oversight of state ES agencies.
- 3) Second Order Devolution New Federalism. Clinton's third-way approach to workforce policies gave preference to local control of workforce policies, sought to incorporate market-based principles into state one-stop delivery systems under WIA, and, after considerable political agitation, strengthened state control of labor exchange policy.

Permissive New Federalism and Labor Exchange Policy

The seeds of Permissive New Federalism in workforce development reform were sown when state ES agencies lost authority to federal–local community action agencies established under EOA (Guttman 1990). In 1973, Nixon approved a job training bill called CETA. This act provided job training funds through block grants to local governments, called prime sponsors. Prime sponsors were responsible for administering the delivery of job training through public and private agencies. According to Guttman (1990), it was recognized that services such as testing, counseling, job referral, and job development under CETA duplicated state ES services, so CETA contained provisions allowing for subcontracting to state ES agencies and requiring coordination. Decisions about how to accomplish subcontracting and coordination were left to local areas with varied results.

In 1978, as part of the renewal of CETA, President Carter supported the Nixon decentralized, local control approach to job training. Under Carter, prime sponsors were encouraged to establish private indus-

try councils that included business representatives to oversee job training priorities and promote employment. During this period, the federal–state structure of the Wagner-Peyser Act remained intact, and the role of state ES agencies was not at the forefront of workforce policy. Carter’s workforce development policy embraced Nixon’s New Federalism, ratifying a bipartisan preference for permissive, decentralized federalism.

Devolution New Federalism and Labor Exchange Policy

The goal of Reagan’s Devolution New Federalism⁶ was to devolve the federal role in the design, finance, and operation of social programs. Reagan was ideologically opposed not only to centralization of the New Deal and Great Society programs, but also to the decentralization of the Permissive New Federalism programs. Dissatisfaction with repeated allegations of fraud and abuse in CETA public service employment and training programs led to enactment in 1982 of JTPA, a trimmed-back version of CETA job training. Under JTPA, state governors “were promoted from merely overseeing the rural ‘balance of state’ [activities] to a dominant position in governing the program” (Mangum 2000, p. 296). Local prime sponsors were reorganized as service delivery areas and job training continued to be delivered by public and private agencies (Balducci and Pasternak 2001).

Incorporation of state ES agencies into job training reform under JTPA was spurred by the politics of limited government. The Reagan Administration and the 97th Congress agreed that to achieve authentic coordination between state ES agencies and local job training agencies, the New Deal era Wagner-Peyser Act required an overhaul. To conform to Devolution New Federalism, Title V of JTPA included makeover amendments to the Wagner-Peyser Act. While the cooperative structure was retained, the amendments to the Wagner-Peyser Act shifted additional authority to states in three ways: 1) they allowed governors extensive discretion in the use of Wagner-Peyser Act funds to administer state ES agencies; 2) they provided for joint planning between state ES agencies and local job training agencies, and the review of both plans by state JTPA councils (which included employers); and 3) they created for the first time a needs-based state allocation formula based on la-

bor force size and unemployment rate. To the extent possible, federal involvement in the planning and administration of job training and ES programs was eliminated.

There is no legislative history explaining what Congress intended when it expanded state authority in the administration of ES programs (Guttman 1990). Perhaps the devolution of authority to states derived from the deregulatory climate of the Reagan era. Ardent USDOL political aides, whose policies reflected Reagan's view of limited government, developed the Wagner-Peyser Act regulations issued in November 1983, and in 1987 supported a bolder legislative attempt by the Reagan Administration to devolve ES as part of the Trade, Employment and Productivity Act. The bill⁷ called for further reduction of federal involvement in the ES system and decentralizing to states ES planning, financing, and administering authority. The 100th Congress did not take action on the legislation. For the remainder of the decade and into the early 1990s, Congress and USDOL had little interest in revisiting the federal-state ES partnership or the role of ES agencies in labor exchange policy.

Second Order Devolution New Federalism and Labor Exchange Policy⁸

Between 1994 and 1998, Congress considered three major workforce development reform bills, each of which included the establishment of a one-stop delivery system to consolidate delivery of workforce development services. The first two bills failed to pass.

The first unsuccessful bill was the Reemployment Act of 1994. This bill reflected the themes of *Reinventing Government* (Osborne and Gaebler 1992), which heavily influenced the early Clinton presidency. The book's thesis is that many public programs could be improved if they competed in the marketplace. The idea of introducing competition into Wagner-Peyser Act service delivery—a concept presented through a series of public consultation papers developed by Clinton policymakers in late 1993 and early 1994—met resistance, with some states and labor unions arguing that the proposal was defective. Among the proposal's defects, three were often mentioned: 1) private agencies were likely to help only those customers who were easiest and most profitable to serve; 2) employer UI taxes were levied to support state ES agencies, not pri-

vate agencies; and 3) competition created duplication of services. Opposition to competition in the delivery of ES services convinced Clinton to modify the competitive model advocated by Osborne and the New Democrats. The modified bill, unveiled in March 1994, ensured that the state ES agency would be a preemptive deliverer of labor exchange services. However, Clinton was unable to marshal broad support for the Reemployment Act, due largely to a preoccupation with complex health care reform. The 103rd Congress ended without decisive action on the bill, and in December 1994 Clinton issued a renewed workforce policy proposal called the G.I. Bill for America's Workers.

In the 104th Congress, legislators passed two versions of workforce development reform: the House version, called the Consolidated and Reformed Education, Employment, and Rehabilitation Systems Act (CAREERS Act), and the Senate version, called the Workforce Development Act. Both bills reflected features of Clinton's policy proposal; however, the bills contained major differences in the division of federal authority between the Secretaries of Labor and Education. The Senate bill also amended section 1 of the Wagner-Peyser Act by deleting the word "public" before "employment offices," which could have resulted in privatizing Wagner-Peyser Act service delivery.⁹ In May 1996, to aid House and Senate deliberations, Clinton defined his views on workforce federalism. In a letter to Congress, he endorsed local control of job training programs, yet he declared that governors should remain responsible for federal grants-in-aid to administer a public ES and should have approval authority over job training plans. Clinton's letter went on to assert that local one-stop centers should be administered by local boards, and job training funds should be allocated to local communities for adults, dislocated workers, and youth (Clinton 1996). The conference bill died when the Senate would not relinquish its view that state governors should be given greater control (Fine 1996).

Finally, a revised bill, WIA (H.R. 1385), was introduced in the 105th Congress on April 17, 1997, and enacted August 7, 1998 (P.L. 105-220), culminating a five-year struggle to achieve workforce development reform. The paramount feature of WIA is that workforce development programs, including ES, must be delivered through local one-stop centers. However, WIA did not change the supervision for the bulk of one-stop services; supervision continues to be divided between state and local governments. Under Title I of WIA, states distribute to local

boards federal job training funds for adults, dislocated workers and youth, and local boards decide how these funds are to be spent. In contrast, state agencies retain responsibility for the administration of federal grants-in-aid for ES and UI programs, and state merit-staff employees deliver ES and UI services.¹⁰

ONE-STOP DELIVERY SYSTEM AND WORKER PROFILING AND REEMPLOYMENT SERVICES

In the early 1990s, states began to consolidate the delivery of workforce development programs. The National Performance Review's (NPR) policy recommendation in 1993 challenged the United States to "(c)reate a system of competitive, one-stop, career development centers open to all Americans" (NPR 1993, p. 49), and in October 1994 USDOL launched the one-stop implementation grant initiative. In the same month, a federal-state work group issued an ES revitalization work plan advocating that state ES agencies be a gateway for workers in the new one-stop system.¹¹ Still, governors were allowed to select the lead agency for the one-stop effort, and between 1994 and 2000, each state received a one-stop implementation grant distributed over a three-year period. The amount of the grant was based on need, and it included no provision to cover ongoing costs. In most states, governors selected their unified workforce development agencies to administer the grants, with state JTPA policymakers often directing the projects.

In 1993, Congress amended the Social Security Act by requiring states to establish a Worker Profiling and Reemployment Services (WPRS) system to identify UI claimants who are likely to exhaust benefits and will need job search assistance and refer them to reemployment services so as to expedite their return to work. By 1996, all states had implemented a WPRS system, with state ES agencies providing the bulk of reemployment services to claimants.¹² Meanwhile, USDOL's welfare-to-work grants, which supported job-finding and placement services for welfare recipients, were directed to JTPA agencies.¹³ Yet, state ES job search workshops grew as a result of the WPRS system, and this growth had a distinct policy consequence: the WPRS system bolstered the case of some USDOL program managers, who in 1997

began advocating for an increase in annual Wagner-Peyser Act funds for reemployment services.¹⁴ During fiscal years (FYs) 2001–2003, USDOL’s annual appropriation included an additional \$35 million in Wagner-Peyser Act funds to provide reemployment services, enabling more UI claimants to be served than would otherwise be possible.

ORIGINAL INTENT OF THE WAGNER-PEYSER ACT AND THE PRIVATIZATION CHALLENGE

In configuring workforce development reform in the 1990s, Democrat and Republican political leaders supported decentralized, local control of state one-stop systems, but they were less certain how to consolidate the administration of ES and job training services. Under WIA, the coexistence of the state ES system and local job training programs has continued, but only after some state and local policymakers sought to decentralize the authority of ES and to contest the delivery of Wagner-Peyser Act services, thereby setting in opposition cooperative federalism and second order devolution. The framework of the original Wagner-Peyser Act was the battleground.

Original Intent and Federalism

The original Wagner-Peyser Act framework as implemented by USDOL consisted of five requirements for a state to become affiliated with the national ES system: 1) establish a state ES agency to cooperate with USES; 2) develop a plan of service; 3) institute a merit personnel system; 4) appropriate matching funds;¹⁵ and 5) appoint an advisory council.¹⁶ The Secretary of Labor was allowed discretion in developing requirements for the receipt of grants. The first three requirements were still in effect during the Clinton era, and debate about the fate of the Wagner-Peyser Act centered on the following three rootstock requirements.

1) Establish a state ES agency. “State legislatures must accept the provisions of the Wagner-Peyser Act and designate or authorize the creation of a state agency to administer” the provisions of the Act (Persons 1934, p. 5). Congress envisioned a strong role for the state agency in

operating labor exchange policy. In fact, the Committee on Education and Labor report that accompanied the Wagner-Peyser Act (S. 510) stated:

We are of the opinion that it is essential that there be a centralized employment service in each State and that it is highly important that there be a coordinated service between the States. This bill proposes a scheme of Federal leadership, with the placement work done by the States, in cooperation with such leadership. (U.S. Congress 1933, p. 4)

2) Develop a plan of service. “[A] plan for the operation of the state ES must be submitted by the state agency and approved by USES” (Persons 1934, p. 5). In 1937, a cooperative agreement between the Secretary of Labor and the Social Security Board provided that USES and the Bureau of Unemployment Compensation act as a single agency in all matters affecting state operations, including development of joint plans of service (U.S. Congress 1964, p. 270). Until the Wagner-Peyser Act amendments of 1982, ES plans were developed with UI plans. Since then, state ES plans have been developed in conjunction with job training agencies. To some degree, this has resulted in a lack of attention to statewide labor exchange policies.

3) Institute a merit personnel system. “[In] the plan of service, the state ES must have agreed to conform to the standards of USES relating to personnel, premises, procedure, and to submit reports on expenditures and operations as required” (Persons 1934, p. 5). Shortly after the Wagner-Peyser Act was enacted, USES adopted a requirement that states must administer a merit personnel system in which appointments and promotions are based upon competence. This requirement ensures that hiring is not affected by patronage, that the execution of program services is impartial and nonpartisan, and that the delivery of services is not affected by favoritism (Balducchi and Pasternak 2001, p. 159). According to Persons (1934), the requirement was a subject of much discussion; yet to ensure the highest quality of state ES operations, USDOL concluded that state staff must be of superb quality and politically impartial. It seemed to USDOL that a merit personnel system—in which individuals are rated objectively on their experience, education, understanding of the job, and personality—was the most reliable means to ensure the highest quality of ES operations.

In sum, the USDOL requirements for the Wagner-Peyser Act mandate that a state agency administer the Wagner-Peyser Act, submit a plan of service to USDOL for approval, utilize a merit personnel system, and deliver Wagner-Peyser Act services using state agency employees. In due course, the market-based urges of New Democrats and Republicans seeking workforce reform were tested against the potency of these long-standing Wagner-Peyser Act requirements. Moreover, the end-of-century march toward workforce development reform raised a high order issue of federalism: whether the federal government has the power to set and enforce requirements upon states in dispensing grants-in-aid to administer programs of a national realm, namely the ES. The federal–state disputes that advanced this issue are described below.

Privatization, State Control, and Labor Exchange Policy

Whether states may delegate the administrative functions of state ES agencies to local boards and allow Wagner-Peyser Act services to be delivered by employees of public or private agencies rather than of the state ES agency (Lazerus et al. 1998, p. 17) became a policy controversy that could have resulted in workforce reform deadlock. The states of Massachusetts, Texas, Colorado, and Michigan introduced alternatives to state ES agency delivery of labor exchange services before USDOL had fully settled on a Wagner-Peyser Act policy of its own making.¹⁷

Massachusetts. In October 1994, Massachusetts received a federal one-stop implementation grant. The grant authorized local boards to contest the delivery of Wagner-Peyser Act labor exchange and job training services, and allowed both public and private agencies to deliver such services. The grant reflected views of USDOL policy officials who sought market competition as a method to raise the quality of services. In April 1998, during the Michigan compliance dispute (see below), USDOL revisited the Massachusetts model and instructed the state to restrict competitive delivery of Wagner-Peyser Act services to four local areas (Boston, Springfield, Cambridge, and Brockton) where it remains.¹⁸

Texas. In January 1996, Texas sought to replicate the Massachusetts model through state legislation. In June, USDOL advised Texas that it should not proceed until a federal policy review was completed.

Further, it warned Texas not to decentralize control of Wagner-Peyser Act funds to local boards or contest the delivery of Wagner-Peyser Act services. At that juncture, USDOL began to weigh the legal and policy merits of privatization as it applied to the Wagner-Peyser Act.

Colorado. In 1997, Colorado was granted permission to devolve the delivery of state ES services to county governments under the authority of its one-stop implementation grant and Wagner-Peyser Act plan of service. In August 1999, Colorado was instructed to ensure that county employees who deliver Wagner-Peyser Act services were protected by a merit personnel system consistent with federal merit staff requirements.

Michigan.¹⁹ Michigan began reorganizing its workforce development structure in August 1997. The confusion caused by an inconsistent federal policy allowing alternative ES delivery structures in Massachusetts and Colorado, contributed to a pitched brawl for intergovernmental control between USDOL and Michigan on whether Wagner-Peyser Act services may be privatized²⁰ (see Appendix 2A). In February 1998, Governor John Engler reorganized Michigan's ES agency by delegating responsibility for the delivery of public ES services to local boards, which were required to administer labor exchange services through competitive contracts with public or private agencies. Further, job seekers and employers were directed to use computerized self-services for most Wagner-Peyser Act services.

Michigan proceeded unilaterally to implement its reorganization²¹ despite notice from USDOL that it should not move forward without approval of a modified Wagner-Peyser Act plan of service or it would risk sanctions. Michigan argued that the Wagner-Peyser Act did not require a merit personnel system. In February, Secretary of Labor Alexis Herman imposed sanctions on Michigan by placing a hold on its letter of bank credit to draw Wagner-Peyser Act funds and putting it on a cost-reimbursement payment system; USDOL also revoked Michigan's one-stop implementation grant. Despite the sanctions, USDOL enabled services to job seekers and employers in Michigan to continue, but a congressional inquiry was held on March 25 to examine USDOL's actions.

The reorganization raised four marquee federal concerns. First, Michigan's reorganization permitted ES services to be delivered by

public or private agencies. USDOL requires that merit-staff employees of a state agency (working in local offices) deliver ES services. Second, the reorganization restricted staff-assisted counseling, job search assistance, and job referrals to veterans, disabled job seekers, and migrant and seasonal farmworkers. Job seekers and employers would be able to access self-services through Michigan’s computer job bank, which was linked to America’s Job Bank (AJB). USDOL contended that such an unbalanced service strategy would undercut the national purpose of the Wagner-Peyser Act: to provide a full-range of Wagner-Peyser Act services that include self-services and staff-assisted services. Third, under Michigan’s proposed “self-services only” approach, it was not clear how ES could identify a job opportunity for a specific UI claimant, refer that UI claimant to a job, and determine the result of the referral. The Wagner-Peyser Act requires state ES agencies to participate in the administration of the UI work test, which often necessitates staff-assisted services. Fourth, the reorganization was executed notwithstanding repeated notice from USDOL that an approved modification of the Wagner-Peyser Act plan of service was needed.

In response to federal sanctions, Michigan sued USDOL, and on May 15, 1998, the U.S. District Court issued an opinion in *State of Michigan v. Alexis M. Herman* (W. D. MI, Southern Div.) granting USDOL’s motion for summary judgment. The court concluded that USDOL’s long-standing construction of section 3(a) of the Wagner-Peyser Act (and the Intergovernmental Personnel Act of 1970) to require merit staffing²² is a reasonable and permissible interpretation of the Act. Michigan filed an appeal and set in motion other intricate political measures to support its case.²³

On July 31, Herman and Engler announced agreement on a framework for the administration of Michigan’s labor exchange program.²⁴ USDOL consented to the delivery of Wagner-Peyser Act services by public agencies other than a state agency, provided that such agencies utilize a merit personnel system and that the provisions of the agreement apply only to Michigan. Michigan agreed to consult with public employee unions in implementing the agreement. As a final point, Michigan agreed to withdraw its appeal of the lawsuit and not to press for other legal, legislative or policy solutions (USDOL 1998). By October, USDOL approved Michigan’s modified Wagner-Peyser Act plan of

service, which incorporated the provisions of the agreement, and lifted sanctions.

Florida. The first consequential post-WIA test of the Wagner-Peyser Act interim regulations occurred in 1999 with legislative actions in Florida. The Florida legislature took up several complicated legislative bills that decentralized responsibility for Wagner-Peyser Act funds to local boards, allowed for competition in the delivery of labor exchange services, and split state responsibility for ES and UI programs between two cabinet departments. During the state legislative process, USDOL raised serious objections to privatization of labor exchange services and, for the first time in the Clinton era, objected to legislative attempts to bifurcate state agency responsibility for UI and ES programs.²⁵ In 2000, Florida enacted the Workforce Innovation Act, creating a single, new state agency (the Agency for Workforce Innovation) to administer WIA, UI, and ES programs without privatizing labor exchange services.

Summary

Prior to WIA, USDOL exercised its administrative authority under section 3(a) of the Wagner-Peyser Act to allow alternative service delivery approaches in three states: Colorado, Massachusetts, and Michigan.²⁶ USDOL is sponsoring a third-party evaluation of the three alternative delivery approaches. In each situation, USDOL is examining different methods of Wagner-Peyser Act service delivery. In Colorado, Wagner-Peyser Act services are delivered through county governments using state and county employees. In Massachusetts, state ES employees deliver Wagner-Peyser Act services except in four local areas where services are delivered by for-profit and nonprofit private and public agencies. In Michigan, Wagner-Peyser Act services are delivered by public employees limited to employees of state government, local units of government, special purpose units of government, school districts, intermediate school districts, public community colleges, and public colleges and universities. Efforts to privatize Wagner-Peyser Act services in Texas and Florida were averted, and in Florida the locus and exercise of authority of the state ES agency were affirmed and the organizational proximity of UI and ES was sustained.

FEDERAL POLICY MAKING: WAGNER-PEYSER ACT AMENDMENTS AND REGULATORY REVISIONS

Separate authorization and distinct funding for Wagner-Peyser Act services were retained under WIA. Yet, Title III of WIA requires Wagner-Peyser Act labor exchange services to be part of state one-stop delivery systems; UI claimants to receive Wagner-Peyser Act reemployment services; and state Wagner-Peyser Act plans to be integrated with state WIA plans. In concert with the development of WIA regulations, revisions to Wagner-Peyser Act regulations²⁷ began earnestly in fall 1998. Interim regulations were issued in April 1999, and final regulations were issued in August 2000.

Throughout the regulatory process, debate ensued over several matters affecting the intergovernmental balance of the federal–state ES structure. These matters focused on the degree of supremacy of the state agency in administering Wagner-Peyser Act funds and the delivery of statewide services in the new, local one-stop delivery systems made up of for-profit, nonprofit, and public service providers. The contenders included New Democrats and Republicans eager to privatize government services, and a dominant faction of federal policymakers attracted ideologically to the federal–local job training structure established under CETA and JTPA. Others were state Wagner-Peyser Act agencies and local boards who vied for authority of Wagner-Peyser Act funds. Still others were labor unions that wielded the clout of the ballot box to uphold the supremacy of the state agency and protect their constituencies.

USDOL made an early tactical decision to make minimal changes to the Wagner-Peyser Act regulations at 20 CFR 652, Subpart A, *Employment Service Operations*, and to place the rules that govern Wagner-Peyser Act amendments contained in WIA in a new regulatory Subpart C, *Wagner-Peyser Act Services in a One-Stop Delivery System Environment*. Policymakers, including an author of this chapter, reasoned that Subpart A contained the long-standing requirements of the Wagner-Peyser Act and to incorporate the new rules into it might place the vital features of the ES program under regulatory scrutiny, especially from those seeking to privatize the delivery of Wagner-Peyser Act services. The tactic proved successful.

Six key federal–state subject areas illustrate new labor exchange policies that arose from amendments to the Wagner-Peyser Act and other federal actions. These labor exchange policies are examined, including descriptions of the contentious issues and the federal policies rendered.

1) Role of the state Wagner-Peyser Act agency and merit-staffing requirements. During the development of the Wagner-Peyser Act regulations, the issues of whether only public employees would deliver Wagner-Peyser Act services and whether the employees would be protected under a merit personnel system were not high-order concerns. As policy matters, these issues were resolved in the Michigan agreement, and USDOL crafted federal interim regulations to ensure uniform application nationwide.

Similar policy clarity was not easily attained with what became the supreme issue of the regulatory process: which levels of subgovernment (i.e., state, county, or city) were eligible to deliver Wagner-Peyser Act services. During 1999 and 2000, the policy choice within USDOL regarding eligible Wagner-Peyser Act service providers whipsawed back and forth between state agencies or all public agencies. In the Michigan agreement, Secretary Herman allowed merit-staff employees of public agencies to deliver Wagner-Peyser Act services, but held that the demonstration only applied to Michigan. However, interim regulations authorized subgovernments to deliver Wagner-Peyser Act services. Prominent labor unions assailed the policy. They viewed the delivery of Wagner-Peyser Act services by subgovernment employees as severely weakening state agency authority. Labor unions charged that allowing merit-staff employees of public agencies to dispense Wagner-Peyser Act services would undermine the supremacy of the state ES agency, and disrupt the statewide delivery of uniform, impartial labor exchange services.²⁸

Interim regulations on the merit-staff issue were crafted by USDOL to serve several policy objectives. USDOL sought to meet the perceived needs of local one-stop delivery systems by allowing multiple public service providers to deliver Wagner-Peyser Act services while preserving the merit personnel requirement. Labor unions precisely identified USDOL's policy intention. They and others charged that the result of this policy would be the unraveling of the single, ag-

gregated state ES agency. To address stakeholders' concerns, USDOL officials met with various groups, including public employee unions that sought meetings to convey their views on behalf of their members. After heated debate, USDOL policymakers resolved that the secretary's declaration in the Michigan agreement that her decision applied exclusively to Michigan meant just that. USDOL declared that employees of a state agency must deliver Wagner-Peyser Act services.

Federal policy. The final Wagner-Peyser Act regulations affirmed that state ES agencies have exclusive authority to deliver Wagner-Peyser Act services through state employees. The policy consequence was nothing less than preservation of a single state agency under the governor's control to administer statewide labor exchange policy.

2) Local ES offices in the one-stop delivery system. At the time WIA was enacted in 1998, the national structure of federal–state ES offices reached nearly 2,400 and each state operated a network of computer job banks linked to AJB. To incorporate the delivery of Wagner-Peyser Act services into local one-stop delivery systems, as required by the amendments to the Wagner-Peyser Act, interim federal regulations stipulated that the state ES agency must make Wagner-Peyser Act services available in at least one comprehensive one-stop center in each local area, and that it may operate other ES offices in each local area as affiliated sites or through electronically connected access points.

This regulation raised inquiries about the nature of affiliated ES offices. In one instance, some of North Carolina's local ES offices were not designated as one-stop centers. The North Carolina ES agency questioned whether it was required to provide a full range of labor exchange services on a full-time basis in all one-stop centers, in addition to its existing, affiliated local ES offices. The interim federal regulations had not contemplated the state ES agency providing only partial services or part-time staffing at comprehensive one-stop centers. During the approval process of North Carolina's five-year WIA and Wagner-Peyser Act plan, USDOL determined that for the one-stop delivery system to be viable in each state, a full range of Wagner-Peyser Act services must be provided on a full-time basis in a one-stop center in each local area.

Federal policy. The intent of federal policy was to require com-

plete consolidation of Wagner-Peyser Act services into the one-stop delivery system. Accordingly, final regulations do not allow states to operate unaffiliated standalone ES offices, and a full range of Wagner-Peyser Act services must be made available during normal and customary business hours in at least one comprehensive one-stop center in each local area.²⁹

3) Responsibility for Wagner-Peyser Act funds. Amendments to the Wagner-Peyser Act under WIA require the state ES agency to participate in the one-stop delivery system and be a member of the state and local boards. The amendments did not alter the Wagner-Peyser Act requirement that vested authority to the state agency designated by the governor to administer Wagner-Peyser Act funds and deliver services. Federal interim regulations reinforced the requirement that state ES agencies retain responsibility for Wagner-Peyser Act funds. During the regulatory comment period, the New York ES agency expressed concern about a state legislature's authority to determine the distribution of Wagner-Peyser Act funds. During the period between issuance of interim and final regulations, this concern made a valuable contribution by helping define USDOL policy in addressing issues raised by the Florida legislature.

During 1999 and 2000, the state of Florida proposed two distinct legislative initiatives (see previous discussion) that attempted to localize the authority of the Florida ES agency and abolish merit staffing. Both legislative proposals conflicted with requirements of the Wagner-Peyser Act and regulations. The proposed Florida legislative actions focused USDOL policy. USDOL took a firm stance that the Florida ES agency controlled the distribution of Wagner-Peyser Act funds and administration of services.

Federal policy. Final federal regulations clarified that the state agency, under the direction of the governor, is responsible for the distribution and oversight of Wagner-Peyser Act funds. However, USDOL stated in the preamble to the regulations that state legislatures have the authority to set priorities for uses of Wagner-Peyser Act funds.

4) Relationship between UI and ES. In the 1990s, WPRS legislation, WIA, and policy stances taken by USDOL strengthened the alliance between UI and ES programs first cultivated by the founders of the federal–state employment security system. Under an amendment to

the Wagner-Peyser Act in WIA, state Wagner-Peyser Act agencies were required to provide reemployment services to UI claimants. In crafting regulations, USDOL anticipated that some state ES agencies might be financially unable to provide reemployment services and included language in the preamble to allow delivery of reemployment services by other service providers. Also, compliance issues that arose in Michigan regarding the delivery of staff-assisted services to UI claimants and the administration of the UI work test prompted the strengthening of Wagner-Peyser Act regulations in these areas.

Federal policy. State ES agencies retain responsibility for the delivery of reemployment services to UI claimants and administration of the work test under state UI laws. In order to ensure that UI claimants receive help to reenter the labor market, other one-stop partners may provide services to them. Subsequently, USDOL policies to promote the use of UI call centers and Internet claims filing may have weakened the relationships between UI and ES, as well as other service providers.

5) Universal access to Wagner-Peyser Act services and methods of service delivery. Since the inception of the Wagner-Peyser Act, a condition of state agency delivery is that services be made available statewide and universally to employers and job seekers eligible to work in the United States. Under Title I of WIA, the requirement of universal access to core (i.e., labor exchange) services was extended to programs that fund services for adults and dislocated workers. During the regulatory process, several stakeholders questioned whether Wagner-Peyser Act funds should provide most of the universal access to core services. Through regulations, USDOL reinforced WIA language to ensure that Wagner-Peyser Act funds would not be the sole support for core services in one-stop centers. This strong federal stance was taken perhaps in recognition of the historic paucity of state Wagner-Peyser Act funds, and to affirm the promise of the one-stop solution.

Another federal issue that arose in the regulatory process was how to integrate Wagner-Peyser Act services and WIA adult and dislocated worker core services. Although WIA defines *core* and *intensive* services, these services are neither defined nor referenced in the Wagner-Peyser Act. In an effort to consolidate service delivery and increase the availability of funds at one-stop centers, USDOL cross-referenced WIA

definitions of core and applicable intensive services in Wagner-Peyser Act regulations.

While Title I of WIA defines two types of job finding services (i.e., core and intensive), the Wagner-Peyser Act regulations require services to be available through three service delivery methods: 1) self-service, 2) facilitated self-help service, and 3) staff-assisted service. The three service methods are closely aligned with WIA core and intensive services. The genesis of the three Wagner-Peyser Act service methods sprang from state Wagner-Peyser Act practices, technological advances in job finding, recommendations of the ES Revitalization work group, and compliance issues that arose in Michigan.

A key provision of the Michigan agreement surrounds the meaning of staff-assisted services. During a meeting between USDOL and Michigan officials on June 25, 1998, Michigan asserted that the requirement of staff-assisted services was met by having “proctors” in one-stop centers’ resource rooms to assist job seekers in the use of self-service job finding software. In response, USDOL averred that Michigan proctors were only providing “facilitated self-help” service and not staff-assisted job finding and placement services. As a result, in the Michigan agreement, USDOL required a Michigan service strategy that included job search assistance and staff-assisted referrals to job openings, in addition to a cadre of “proctors” providing facilitated self-help services. Wagner-Peyser Act regulations were crafted to make a clear distinction between facilitated self-help service and staff-assisted service methods.

Federal policy. Regulations require state ES agencies to provide three methods of service delivery (cited above) in at least one comprehensive one-stop center in each local area. Services must be available statewide and their application should be described in state and local WIA memoranda of understanding. Also, each one-stop partner in the comprehensive one-stop center must make available the core services of its program. It is USDOL’s contention that funding core and intensive services under both WIA and the Wagner-Peyser Act enables state and local boards to make choices that maximize the use of funds.

6) State plans. Prior to the Wagner-Peyser Act amendments of 1982, state UI and ES programs prepared joint, yearly planning documents to coordinate the delivery of services to job seekers, UI

claimants, and employers. These plans, called the Program Budget Plan, were submitted to USDOL to ensure compliance with federal requirements and national policy priorities. Beginning in program year 1984, Wagner-Peyser Act requirements were revised to require state ES plans to be developed jointly with JTPA programs. Over the years, annual state ES plans³⁰ became flat and pro forma.

Under WIA, states are required to submit five-year plans. During the regulatory process, USDOL made two determinations that impacted state Wagner-Peyser Act plans. The first decision was that Wagner-Peyser Act plans must be functionally integrated within states' strategic WIA or unified plans. State governors are not permitted to submit their statewide Wagner-Peyser Act plans as separate components of a joint plan; instead they must be submitted as integrated documents. Secondly, integrated WIA and Wagner-Peyser Act plans are developed for five years without annual updates, notwithstanding changes in the organization of the states' workforce structure or levels of performance. In our view, these decisions have produced state WIA and Wagner-Peyser Act plans that are compliance documents rather than strategic blueprints, and states would be better served if five-year plans were required to be updated annually.

Federal policy. To ensure a collaborative planning process between state boards and state ES agencies, federal regulations require states to submit integrated plans encompassing Title I of WIA and Wagner-Peyser Act programs. States may utilize either of two planning documents: 1) Strategic Five Year State Plan for Title I of WIA and the Wagner-Peyser Act, or 2) State Unified Plan.

Regulatory Shifts in Workforce Federalism

During the initial two eras of New Federalism, USDOL abrogated to states much policy and program control of Wagner-Peyser Act service delivery. Federal Wagner-Peyser Act regulations in 1983 devolved authority of labor exchange policy to state control, and regulations were intentionally silent on issues of national sovereignty (e.g., services and merit standards). The federal–state ES program tilted toward states in the spirit of New Federalism. Job training programs began to dominate the workforce development scene, and funds shifted to local job training agencies.

In 2000, USDOL failed to hardwire the vision of some New Democrat and Republican policy makers at each level of government who sought local control of Wagner-Peyser Act policy. Supporters of local control argued that it is sensitive to labor markets, is innovative and promotes stronger employer involvement. Backers of state control asserted that to ensure impartial and equitable service delivery statewide, a state agency under the direction of the governor must administer Wagner-Peyser Act policy.

The triumph of cooperative federalism over second order devolution thwarted attempts to push Wagner-Peyser Act authority through the knothole³¹ of state government to local agencies. Revised Wagner-Peyser Act regulations reversed 15 years of federal inaction in the oversight of labor exchange policy, and new regulatory provisions recognized the exclusive authority of the state ES agency and prescribed service and merit requirements that supported that authority. The requirement of a merit personnel system ensures the solidarity of a single state agency to administer labor exchange policy at the local level. Without it, statewide labor exchange policy would likely be diffused among local boards and lose its state composition. A single state Wagner-Peyser Act agency provides state governors with the power to reach down to their local communities to direct labor exchange policy. Workforce federalism shifted labor exchange policy in four areas:

- 1) Rather than devolve state agencies' authority over Wagner-Peyser Act funds and services to the control of state and local WIA boards, federal regulations strengthened the authority of state ES agencies.
- 2) The Wagner-Peyser Act regulations of 1983 were silent on many issues of state agency administration. Similarly, amendments to the Wagner-Peyser Act in WIA did not include changes to state authority, merit personnel protection, or coordination with UI. However, challenges during the 1990s to USDOL's authority to set conditions and enforce them on states required the Wagner-Peyser Act regulations of 2000 to strengthen the federal-state ES program in those areas.
- 3) Under Title I of WIA, the principle of universal access was expanded beyond the Wagner-Peyser Act to include adult and dislocated worker programs. In the Wagner-Peyser Act regula-

tions of 2000, USDOL mandated that Wagner-Peyser Act services include three distinct service delivery methods (i.e., self-service, facilitated self-help, and staff-assisted services) to meet the needs of a statewide labor exchange structure.

- 4) The state ES agency was not designated in WIA to administer the one-stop delivery system, although it is required to be a partner in the system and provide a full-range of Wagner-Peyser Act services in at least one comprehensive one-stop center in each local area.

LABOR EXCHANGE POLICY CHALLENGES

An emerging federal issue in the reauthorization of WIA in 2003 indicates a new challenge for U.S. labor exchange policy. Some believe that WIA failed to provide state governors with sufficient power to direct state job training and economic development policies within states because WIA funding formulas mandate that most job training funds go to local areas. The ascendancy of governors in WIA may be an issue of hefty political debate and thus could signal the twilight of second order devolution and local control of workforce federalism.

On the other hand, the Bush Administration's FY 2003 budget included a far-reaching UI/ES reform proposal dubbed "New Balance." Introduced in September 2002, the New Balance bill (H.R. 5418) proposed to add a new player to the federal–state–local relationships: the state legislatures. Under the bill, the federal government would no longer provide funds to administer services under the Wagner-Peyser Act; instead, financing of ES and UI programs would be shifted to states through a multiyear phase-out of 75 percent of the *federal* unemployment tax paid by employers. The new player—the state legislatures—would have the potential to increase or reduce the funding of state ES programs by requiring governors to justify their funding requirements.

While the bill is a vestige of Reagan-era Devolution Federalism, it is motivated by two decades of complaints by the states and employers about inadequate funding of ES and UI administrative expenses. Concurrent to the underfunding of administrative expenses, employer UI

taxes have generated large balances in the UI Trust Fund. Further, some employers have been effectively double taxed by states supplementing ES and UI funds. In devolving the financing of ES and UI programs to the states, the New Balance bill requires states to continue labor exchange services. However, it does not ensure that state legislatures would authorize funds to maintain state labor exchange operations at current levels. As of this writing, the New Balance bill was not reintroduced in the 108th Congress.

WIA Reauthorization

In its FY 2004 budget request, the Bush Administration continues to press for fundamental changes in the administration of labor exchange policies. The authorization of WIA expires on September 30, 2003, and a provision in President Bush's proposal³² to consolidate Wagner-Peyser Act and WIA Adult and Dislocated Worker funding streams is intended to integrate the majority of services at one-stop centers. To accomplish this, the Bush proposal would repeal the long-standing Wagner-Peyser Act and incorporate some of its features into WIA. The funding for core services of one-stop centers would be provided to states and local areas through one consolidated block grant. Federal funds would be derived from general revenues appropriated by Congress. If enacted, this provision would unravel the mutual funding of UI and ES services through the UI trust fund. However, efforts in Bush's companion bill (H.R. 444, "Back to Work Incentive Act") to promote the use of Personal Reemployment Accounts to UI recipients who need the most help in getting back to work may increase the use of some labor exchange services, such as job placement.

Nonetheless, Bush's proposal raises as a prime issue the distribution of power between state governors and local leaders for control of labor exchange policy. Currently, Wagner-Peyser Act funds are retained at state levels under the purview of governors. Under the Bush proposal's consolidated funding approach, 50 percent of the combined adult funding stream must be sent to local areas according to statutory distribution. Hence, in comparison to the Wagner-Peyser Act, state governors could lose authority over the bulk of their labor exchange funds and, as a possible consequence, their ability to steer labor exchange policies statewide. This provision may be contested in the enactment process.

While it is too early to predict the consequences of most provisions in the Bush proposal, the provisions would clearly provide for greater flexibility in the use of labor exchange funds by local areas. Conversely, they would nullify the public charter of ES, allow private service providers to deliver labor exchange services, and may hamper the coordination of labor exchange and UI services.

SUMMARY

This chapter tracked federal–state relations in labor exchange policy throughout the life of the Wagner-Peyser Act. During the first 35 years of the act, efforts to shift the federal–state balance of power were directed at “federalizing” the program; during the last 35 years, efforts were directed at “localizing” it. Beginning in the 1970s and throughout the three eras of New Federalism, weak federal stewardship of the Wagner-Peyser Act was noticeable in reduced Wagner-Peyser Act grants-in-aid, as well as in ambivalence and skepticism toward labor exchange policy. At the same time, the role of local job training agencies was nurtured and training grants-in-aid were increased.

During these eras, there was a preference for local control of workforce development programs. In 1978, Carter affirmed the primacy of local control by embracing the Nixon federal–local job training arrangement, and in 1996 Clinton reaffirmed it as a matter of public approbation. Through the one-stop solution, Clinton devised a “third-way” approach to workforce federalism that ultimately did not reappropriate political control of ES and job training programs. The role of governors in administering labor exchange policy was strengthened, and state ES agencies and local job training agencies were fastened together by local one-stop delivery systems. The effect of the third-way approach on statewide labor exchange policy outcomes is as yet unknown. As the new century beckons new approaches to labor exchange policy, we make the following observations:

- Fragmented governance is the result of local workforce federalism, and it appears to foster intrastate rivalries and fragmented delivery of workforce services.

- Despite the federal–state character of ES programs, local workforce federalism has sometimes precipitated uneven labor exchange services from one-stop center to one-stop center within states and across states.
- Local control of workforce programs may have inhibited the ability of state governors to connect economic development and workforce development in local areas.
- At the end of the 20th century, federal–state conflicts in grants-in-aid policy under the Wagner-Peyser Act established that states do not have the right, absent federal approval, to subrogate to subgovernments or private agencies funds for administration or delivery of labor exchange services.
- Merit personnel requirements help ensure the continuity of a single state Wagner-Peyser Act agency and the equitable delivery of labor exchange services statewide.

The journey of the Bush presidency perhaps bids another turn of federalism’s historic wheel as it applies to labor exchange policy. President Bush’s New Balance bill and WIA reauthorization proposal would shift some workforce development control to state governors, but would dismantle the New Deal era administrative structures of ES and UI programs. As in the past, centralization, and decentralization³³ will continue to pose splendid tensions in U.S. workforce federalism.

Notes

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1. The Great Depression, according to Humphrey (1970, p. 47), necessitated expansion of the federal role through preventive measures (e.g., national employment system) as well as other corrective interventions. Humphrey explains the federal government’s new purpose during the 1930s by excerpting from Roosevelt’s October 1936 address at Worcester, Massachusetts, a quote from Lincoln: “The legitimate object of government is to do for the people what needs to be done but which they cannot by individual effort do at all, or do so well, for themselves.”

2. While federal grants-in-aid mushroomed in the 20th century, the first grants to states were under the Articles of Confederation, when in 1785 Congress earmarked a section of every township in the federal territory for the support of public schools (Vines 1976, p. 14).
3. In 2003, grants are allotted to states by USDOL under a formula at section 6 of the Wagner-Peyser Act that distributes 97 percent of the annual ES appropriation according to each state's relative share of the civilian labor force and number of unemployed workers. USDOL distributes 3 percent of the total available ES funds to states to assure maintenance of statewide ES systems. Ninety-seven percent of state ES grants is derived from the Federal Unemployment Tax Act, an employer-based tax, and 3 percent is derived from general tax receipts.
4. The adoption of a federal–state structure for the ES program in 1933 may have helped sway politicians to select an identical arrangement in 1935 for the UI program (Blaustein 1993, p.137).
5. In 1966 the U.S. Senate passed a bill (S.2974) to reform the Wagner-Peyser Act and make ES agencies the centerpiece of a comprehensive manpower system. The House did not take up the bill because the bill mandated the separation of ES from UI and increased the authority of the federal government in state ES activities (Guttman 1990).
6. Barnow (1993, p. 94) and King (1999, p. 63) refer to workforce development after 1978 as “coercive federalism,” where the federal government offers states greater authority but adds significant constraints. Labor exchange policy was established during the period of cooperative federalism, and the basic requirements of the Wagner-Peyser Act remain unchanged. Therefore, as labor exchange policy applies to federalism, we do not refer to it as coercive.
7. Introduced in February 1987 by Representative Michael (H.R. 1155) and Senator Dole (S.539), the bill at Title I, Subtitles F and G contained the Employment Security Financing Act of 1987 and the Employment Services Act of 1987, expanding the role of governors and the private sector in ES activities. While the legislation garnered only 30 House cosponsors and 2 Senate cosponsors, it did spotlight a political trend toward decentralized governance.
8. This section draws from Balducchi, Johnson, and Gritz (1997) and Balducchi and Pasternak (2001).
9. If enacted, the amendment may have raised serious accountability, equity, and continuity of service issues in the statewide delivery of impartial labor exchange services. However, the amendment did express the views of some policymakers at each level of government who wanted USDOL to liberalize restrictions on the uses of Wagner-Peyser Act funds.
10. Except in the cases of Colorado, Massachusetts, and Michigan, where demonstrations of alternative delivery systems are under way.
11. The work group's vision statement declared, “The ES is the Nation's recognized leader in providing labor exchange services and a universal gateway to workforce development resources by professional, empowered employees” (USDOL 1994).

12. In over two-thirds of states, ES was the major provider of reemployment services, serving more than 75 percent of UI claimants (USDOL 1999, p. II-14).
13. Politicians viewed Temporary Assistance for Needy Families as a state program and welfare-to-work as a local program. Mayors and county officials argued that hard-to-serve welfare recipients reside in urban areas, and USDOL grants should be under their control (Uhalde 2002).
14. In October 1997, the Employment and Training Administration issued policy guidance to state ES agencies to spur growth of reemployment services to UI claimants (USDOL 1997).
15. A matching requirement was placed in the original act in some measure to take advantage of state funds in 23 states that already operated ES offices. The requirement was in effect until federalization of the ES in 1941 and not resumed when Congress returned the ES to federal–state administration in 1946 (Haber and Kruger 1964, pp. 27 and 35). In 1950, the Wagner-Peyser Act was amended to eliminate the matching provision.
16. The original language of the Wagner-Peyser Act required states to appoint advisory councils composed of employers, workers, and the public to formulate labor exchange policies. In 1939, through presidential order, USES and the Bureau of Unemployment Compensation were merged in the Social Security Board to form the Bureau of Employment Security, and the scope of federal and state advisory councils was broadened to include the formulation of UI policies.
17. USDOL did have an initial policy position on competition in one-stop center operations, and the Massachusetts model reflected the views of high-level White House and USDOL officials. USDOL’s policy changed over time, and formal ETA policy was established in the Wagner-Peyser Act regulations of 2000.
18. Early results of the Massachusetts demonstration are varied. Drake Beam Morin, a for-profit placement firm, dropped its contract to deliver services at the JobNet Boston one-stop center when it could not select job seekers to serve and meet profit expectations (Westat, Inc. 2001).
19. This section is drawn from Balducchi and Pasternak (2001).
20. Palmer (2002) asserts that the basis for Michigan’s reorganization was inadequate federal ES funding, the prospect of cost savings through competitive selection of service providers, and expansion of service access points and technology.
21. According to Palmer (2002), Michigan proposed to exercise the flexibility it believed it had under existing federal law and policy to “utilize a combination of state government, local government, and private entity-provided services to carry out the Wagner-Peyser Act and meet employer and job seeker needs in accordance with state needs and priorities.”
22. In 1935, USDOL suspended Missouri’s Wagner-Peyser Act grant for violation of merit staffing under section 3(a) of the Wagner-Peyser Act. A USDOL letter dated August 24, 1935, to Missouri (apparently based upon a USDOL solicitor’s opinion of March 7, 1935, sent to Iowa) was included in USDOL’s court brief. Although USDOL also argued that Michigan had violated section 5(b) of the Wag-

- ner-Peyser Act, the court ruling was based solely on section 3(a) as cited in the Missouri precedent. As far as we know, the Michigan compliance dispute marked only the second instance of sanctions under the Wagner-Peyser Act imposed upon a state.
23. Congress advised USDOL to work out an agreement with Michigan. Both Michigan and organized labor could have blocked Senate passage of the workforce development bill (Uhalde 2002).
 24. Engler and Herman met on July 23, 1998. Engler did not come to the meeting with a compromise proposal; he recalls that the agreement was developed at the meeting. Herman and Engler met alone in a small library adjacent to the Secretary's office (Engler 2002; Uhalde 2002).
 25. USDOL did not raise a legal objection to Missouri's 1999 reorganization that separated UI and ES agencies but did not privatize ES activities. The authors believe in the importance of close linkages between UI and ES activities, and that such linkages are generally achieved under the aegis of a single agency. In a letter to Florida, USDOL (2000) stated, “. . . (A)s a policy matter, the State should appreciate the centrality to the One-Stop delivery system of the administrative relationship between Wagner-Peyser Act services and UI services.”
 26. USDOL permitted Massachusetts and Colorado to use alternative service delivery approaches under the authority of their one-stop implementation grants, which were distributed to states under Wagner-Peyser Act authorization. Prior to its one-stop implementation grant, Colorado utilized limited county-based delivery of services consistent with its Wagner-Peyser Act plan of service. Michigan received permission to use alternative service delivery approaches through its Wagner-Peyser Act plan of service. The statutory authority that allows for alternative delivery approaches is section 3(a) of the Wagner-Peyser Act.
 27. Administrative regulations at 20 CFR 652 are rules that implement Wagner-Peyser Act provisions and establish federal requirements for receipt of Wagner-Peyser Act funds. Policy directives are ETA program guidelines issued to state ES agencies.
 28. Public employee unions raised a residual concern over the degree of supervision that private or other public one-stop operators could exercise over state Wagner-Peyser Act employees. The Service Employees International Union (1998) stated, “private supervision of the employment service creates an opportunity for the diversion of public resources to further private interests.” Early in the process, federal policymakers determined that private or other public agency one-stop operators must dispense only guidance to state Wagner-Peyser Act employees in administering labor exchange services. The term *guidance* was not defined in federal regulations or subsequent policy directives.
 29. One result of these decisions has been that in some local areas of a number of states, one-stop centers and ES offices are located near each other, which might be redundant. It would be interesting to know why in some instances customers prefer to go to ES offices rather than nearby one-stop centers selected by local boards, and in other instances the opposite.

30. USDOL's appropriation laws for FYs 1996–98 contained language, incorporated in WIA, which enabled states to seek waivers of ES plan requirements at section 8 of the Wagner-Peyser Act. Requests for waivers of the plan requirements at section 8 and of the audit and reporting requirements at sections 9 and 10 were scantily requested, as they were ministerial in nature or rendered moot by virtue of other federal requirements that prohibited granting of such waivers.
31. We refer to this as *Knothole Federalism*. A knothole is used as a metaphor to illustrate this trend in federalism. In the case of WIA, state entities responsible for job training programs act as wooden planks through which the federal government punctures a knothole in state authority to pass federal policy and funds to local boards and operating entities.
32. On March 13, 2003, Representatives McKeon (R-CA) and Boehner (R-OH) introduced H.R. 1261, "Workforce Reinvestment and Adult Education Act." H.R. 1261 was not the Bush Administration's bill, but its provisions were substantially similar to the Bush proposal.
33. Interestingly, Block (1993, p. 103) suggests that "... decentralization often has the opposite effect of its intention" as each new self-ruling division begins recreating within itself the ethos of the larger organization that was taken apart.

Appendix 2A
**Reorganization of the Michigan Jobs Commission:
 Chronology & Anatomy of a Wagner-Peyser Act
 Compliance Dispute**

| DATE | ACTIONS |
|----------|---|
| 8/6/97 | John Engler, Governor of Michigan, issues Executive Order 1997-12, which sets in motion reorganization of the Michigan Jobs Commission (MJC). |
| 8/18/97 | Letter from Melvin Howard, Acting ETA Regional Administrator, to Douglas Stites, MJC Chief Operating Officer, raises questions relating to federal requirements. |
| 9/12/97 | Letter from USDOL to Douglas Rothwell, MJC Chief Executive Officer, advising MJC to suspend implementation and submit Wagner-Peyser Act plan and one-stop grant modification. |
| 9/30/97 | MJC shares draft Wagner-Peyser Act plan modification with USDOL at Washington, DC, meeting. USDOL indicates that merit-staffing requirements apply to Wagner-Peyser Act services. |
| 10/6/97 | Letter from USDOL to Rothwell regarding effects of reorganization on UI program. USDOL sets forth Wagner-Peyser Act requirements that include UI work test and reemployment services provisions. |
| 10/21/97 | Letter from USDOL to Stites commenting on draft Wagner-Peyser Act plan modification and requesting submission of One-stop plan modification. USDOL describes areas of deficiencies with MJC reorganization. |
| 10/31/97 | Letter from Stites to Raymond Uhalde, Acting ETA Assistant Secretary, responding to October 6 letter and informing USDOL that UI claimants will register for work via America's Talent Bank. |
| 11/17/97 | Engler issues Executive Order 1997-18, which completes the MJC reorganization. |
| 12/8/97 | USDOL receives formal copy of Michigan's Wagner-Peyser Act modification, which is identical to draft modification. Letter from Stites to Uhalde addresses Wagner-Peyser Act issues raised in October 21 letter. |
| 12/24/97 | Letter from USDOL to Rothwell advising that the Wagner-Peyser Act plan modification will not be approved, describing deficiencies in the plan modification, and requesting its withdrawal. |

- 12/30/97 MJC withdraws its request for a Wagner-Peyser Act plan modification. During this period, Alexis Herman, USDOL Secretary, contacts Engler by telephone to discuss the MJC reorganization.
- 1/21/98 MJC officials attend meeting at USDOL to discuss major issues, including merit staffing and over-reliance on computer self-services. USDOL offers potential opportunity for sub-state pilots of alternate delivery systems. MJC officials indicate that they will apprise Engler and get back to USDOL.
- 1/30/98 Herman contacts Engler by telephone to notify him that issues remain unresolved.
- 1/30/98 Two letters from USDOL to MJC: 1) Uhalde to Rothwell stating that unless ETA receives notification from MJC that reorganization will be suspended on February 2, Wagner-Peyser Act and one-stop grants will be adversely affected; 2) Howard to Stites stating that Wagner-Peyser Act plan modification must be approved prior to implementation of reorganization. USDOL prepares to freeze MJC's drawdown authority, provide reimbursement for only approved Wagner-Peyser Act activities, and terminate Michigan's one-stop grant.
- 1/30/98 Letter from Stites to Uhalde resubmitting Wagner-Peyser Act plan modification without changes required by USDOL.
- 2/2/98 Stites informs Howard by telephone that MJC is going to execute the reorganization plan. MJC files motion for temporary restraining order and order to show cause in U.S. District Court.
- 2/3/98 Two letters from USDOL to MJC: 1) Howard to Stites to withhold drawdown authority until modification to Wagner-Peyser Act plan; 2) Janice Perry, ETA Grant Officer, to Stites notifying MJC that (a) second year One-stop grant funds denied, and (b) first year funds not available after February 2, 1998.
- 2/6/98 Preliminary hearing held in U.S. District Court in Grand Rapids, MI, before Judge Robert Holmes Bell.
- 2/10/98 Bell denies MJC's request for injunction against USDOL actions. Sets April 15 to hear merit-staffing issue. (Hearing subsequently postponed until May 1, 1998.)
- 2/27/98 Letter from Howard to Stites denying approval of January 30 Wagner-Peyser Act plan modification.
- 3/13/98 USDOL and MJC file briefs on merit staffing in U.S District Court.
- 3/25/98 Uhalde testifies before Rep. Hoekstra's (R-MI) Subcommittee on Oversight and Investigation.

- 3/26/98 Letter from Stites to Uhalde addressing issues raised in February 27 disapproval letter.
- 4/1/98 ETA officials meet with Stites and John Palmer, MJC ES Director, in Washington, DC, to clarify issues and seek resolution of concerns outside of the merit-staffing issue.
- 5/1/98 Bell holds a hearing on the merit-staffing issue.
- 5/15/98 Bell issues an opinion and an order granting USDOL’s motion for summary judgment. The court upholds USDOL’s position on merit staffing, indicating that it “is neither arbitrary or capricious nor in excess of the Department’s authority.”
- 6/12/98 Letter from Byron Zuidema, ETA Regional Administrator, to Stites denying Michigan’s PY 1998 Wagner-Peyser Act plan. Issues unresolved: 1) merit staffing; 2) stakeholder input; 3) UI work test; 4) universal access to computer self-services; 5) program data reports; 6) staff-assisted job search assistance; and 7) VETS concerns.
- 6/23/98 Letter from Palmer to Zuidema requesting reimbursement of \$2.9 million for February 1998.
- 6/25/98 Stites and Palmer meet with Uhalde, John Beverly, USES Director, and David Balducchi, USES Chief of Planning and Review, in daylong dialogue to bring Michigan’s Wagner-Peyser Act plan into compliance.
- 7/23/98 Herman and Engler meet at USDOL to discuss the MJC issue.
- 7/31/98 Herman and Engler announce a resolution to the dispute and a framework for the administration of Michigan’s ES program. MJC agrees to drop judicial, legislative and policy actions.
- 8/12/98 Letter from Stites to Zuidema submitting revised Wagner-Peyser Act plan.
- 8/20/98 Uhalde meets with Stites and stakeholders in Lansing, MI, to discuss implementation issues and obtain stakeholder input.
- 9/2/98 Letter from Zuidema to Stites raising issues with revised Wagner-Peyser Act plan.
- 9/10/98 Letter from Stites to Zuidema addressing September 2 letter. USDOL not satisfied with response.
- 9/13/98 Kitty Higgins, USDOL Deputy Secretary, meets with labor union leaders from AFL-CIO, AFSCME, and SEIU regarding implementation of the Michigan agreement.
- 9/16/98 Letter from Zuidema to Stites requesting additional time (no later than September 30, 1998) to resolve four outstanding issues: 1) presence of at least one state merit-staffed employee in each workforce area to perform UI work test; 2) accelerating

- commencement of staff-assisted services; 3) content and submission of transition plan; and 4) performance benchmarks. Letter declares that MJC may treat this as a denial of plan submitted August 12. Letter authorizes reimbursement of \$2.9 million for February 1998 Wagner-Peyser Act costs.
- 9/18/98 Letter from Stites to Zuidema addressing the four issues raised in September 16 letter. USDOL not satisfied with response.
- 9/21/98 Conference call between Beverly, Balducchi, Stites and Palmer to clarify the four issues raised in the September 16 letter. Achieve potential resolution of issues regarding staff-assisted services, transition plan, and performance benchmarks; however, no resolution of UI work test issues.
- 9/25/98 Higgins meets again with union leaders (same participants as September 13 meeting). Unions express dissatisfaction with September 16 letter from USDOL to MJC (releasing funds) and indicate that former state ES employees are not receiving an opportunity to fairly compete for jobs.
- 9/25/98 Herman calls Engler to relate that agreement has broken down and MJC needs to be flexible.
- 9/29/98 Uhalde and Beverly travel to Lansing, MI, to discuss terms of agreement with MJC and union leaders.
- 10/13/98 Letter from Stites to Zuidema providing sufficient information to resolve remaining four issues.
- 10/14/98 Letter from Barry Dale, ETA Regional Grant Officer, to Stites indicating that October 13 letter fully resolves issues and Michigan's PY 1998 plan is approved. Letter removes reimbursement provision on remaining PY 1996-97 Wagner-Peyser Act expenditures and enables MJC to again draw down Wagner-Peyser Act funds.
- 10/30/98 USDOL restarts Michigan's one-stop grant for second and third years.
- 11/3/98 MJC effectuates one-stop agreement.

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