American Experience with Workforce Investment Grants: Food for Thought for European Social Fund Planners

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(1) I am pleased to attend the conference "Shaping the Future of the ESF: ESF and Europe 2020," and I am honored to think someone believes I might have something useful to contribute. This note begins the search for that something. I first summarize what I know about the European Social Fund and the motivation for this meeting. Then I turn to a review of what may be a pertinent American policy experience.

The Little I Know

(2) Bear with me while I rehearse my limited knowledge. As originally conceived, the European Social Fund (ESF) provided financial support for Member State (MS) vocational training programs with the intent of improving workers' mobility and employment opportunities. The scope of and procedures for ESF activity have changed substantially as the size and ambition of the EU has grown, especially in the wake of the 2000 Lisbon Summit and Nice Council. Currently the ESF essentially translates the European Employment Strategy into grants-in-aid for MS projects that are consistent with EU priorities for employment and social inclusion. Funding in the present (2007-2013) cycle amounts to €75 billion and accounts for about 10 percent of the entire EU budget.

(3) There are six ESF funding priorities for the present cycle:

- Improving human capital (34% of total funding)
- Improving access to employment and sustainability (30%)
- Increasing the adaptability of workers and firms, enterprises and entrepreneurs (18%)
- Improving the social inclusion of less-favoured persons (14%)
- Strengthening institutional capacity at national, regional and local levels (3%)
- Mobilisation for reforms in the fields of employment and inclusion (1%)

(4) Beyond these priorities, ESF projects are targeted at particular classes of people believed most vulnerable to unemployment and social exclusion. Lists of targets vary, but typically include the unemployed (especially long-term unemployed), economically inactive, older persons, women, young people, persons with disabilities, and other disadvantaged groups. These are people targets, but the ESF also supports development and modernization of educational "structures and systems"—that is, institutional capacity.

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(5) €75 billion is not, to use a term common in Arkansas when I was a boy at the time of the Treaty of Rome, "chicken feed." But it is very small compared to MS budgets for employment and training activities. Thus, the object of the program cannot be simply to fund such activities, but rather to influence their content and direction. In the context of the theory of intergovernmental assistance, when we encounter grants-in-aid programs of this type, we look for justification either on grounds of redistribution of resources or correction of externalities. The ESF involves a good deal of redistribution (poorer member states receive a share of funds disproportionate to their populations). But the program also seems intended to signal desirability of certain types of expenditures beyond what MS would spend had they the Euros without strings attached. This desirability springs from benefits received by EU citizens other than those of the MS gaining the grant. An EU neophyte like me, when confronted with something like the ESF, tries to identify just what those external benefits are, and then puts on his "public management" hat to think about how to maximize the value of such benefits per Euro expended. However, any recommendations would be complicated by the multiplicity of social fund objectives.

(6) We are in Brussels to discuss the next funding cycle, a cycle that ends in 2020. We have five big issues on the table: (1) what is the "added value" of the ESF, (2) what should the ESF support, (3) where should the ESF operate, (4) how should the ESF be delivered, and (5) how should the ESF relate to other European Union instruments? It's not at all clear to me what experience gained elsewhere has to offer. I take my cue from three ESF features: (1) the employment/human capital orientation, (2) the strategic rather than comprehensive character of funding, and (3) the targeting of specific groups. In the United States, activities funded under the Workforce Investment Act (WIA) sound much the same. Despite this resonance, there are important differences. It will be a challenge to uncover relevance to the five ESF issues, but I will argue that there are some and, moreover, there are important lessons for WIA from the ESF.

The Workforce Investment Act

(7) In the US, employment and training services for workers are provided by a variety of public and private organizations. Traditionally the federal government has funded employment-related services that are delivered by state-managed agencies. In 1988, the Workforce Investment Act (WIA) created a new, more integrated training and employment assistance system by adding to and broadening the range of federally-sponsored employment and training services already available, co-locating them at "one-stop" centers throughout the country, and establishing a local area management system structured to be more responsive to employer needs. The legislation created three new programs—Adult, Dislocated Worker, and Youth. (A "dislocated worker" is a person who either left or lost a job because the employer closed, relocated, abolished their position or shift, or did not have enough work to give the employee.) Workforce services are provided by about 3,000 one-stop career centers located throughout the country. One-Stop operations are guided by local Workforce Investment Boards operating under state supervision. At the federal level, WIA activities are the responsibility of the Department of Labor (DOL).

(8) For adults and dislocated workers, WIA provides what are referred to as "core", "intensive", and "training" services. Core services are traditional employment service activities such as provision of labor market information and other resources for job search. Much of this occurs through self-service or with minimal staff input. More staff

input occurs with intensive services such as detailed needs assessment and case management. Training services include the usual occupational skills and on-the job efforts. The youth program offers ten types of services without the core-intensive-training distinction. While all workers can receive core services, state workforce agencies determine which workers receive intensive and training services and the mix of services those selected receive.

(9) WIA is wholly federally funded. Funding is by category (youth, adults, dislocated workers) and amounts are distributed across states based on formulas that reflect population, the numbers of unemployed, and, to a modest extent, size of the low-income population. Similar procedures govern distribution within states. The total budget for 2010 was about $4.2 billion for the formula grants, the employment service, and related education programs; roughly $2.8 billion additional was added in 2009 as part of the economic stimulus package. WIA was designed to promote greater accountability in federal workforce programs by establishing new performance measures. There are 17 such measures: 4 for the adult programs, 4 for dislocated workers, 7 for youth, and 2 general measures of "customer satisfaction." The primary source for tracking employment outcomes is Unemployment Insurance (UI) wage records. Take note of scale here: Abstracting from the stimulus, WIA spends about $4.2 billion per year for a total population of 310 million and this includes the employment service. The ESF spends about €10 billion a year—$12.4 billion at this month's exchange rate (sorry)—for a total population of 500 million, and as I've already noted, most MS employment services are not ESF funded.

(10) To receive each year's formula allocation, states must submit a plan and negotiate performance targets with the appropriate regional DOL office. Regional staff has the task of negotiating targets with the states based on factors that affect performance but are beyond their control—high unemployment levels or serving a more disadvantaged population, for example. The negotiation process is intended to "level the playing field" between states, so that interstate comparisons are made not on the basis of absolute performance but performance relative to targets negotiated for circumstance.

(11) At least at first blush, there are points of overlap between what the ESF does and WIA. Both have as a central focus employment. Both have target groups. Both are concerned with outcomes and with institutional development. Both involve a fiscal and a guiding relationship between a central government and diverse member states. Nevertheless, the differences are profound. The scope of ESF activities is much broader—to my knowledge, no one at DOL has ever mentioned "social inclusion." But the most important difference is the funding relationship. In principle, the ESF provides grants for activities that the MS wouldn't otherwise undertake—these efforts come in addition to the core state-funded employment services. WIA funds the entire service; it is the states' responsibility to administer the program. The boundaries of WIA activities are well-defined, and in consequence expenditures are much more easily audited than are outlays for the diverse projects supported by the ESF. While states carp about details of federal regulation, subsidiarity is less of an issue when all funds come from Washington. And since the formula grants include administrative costs, it is hard to raise proportionality issues. Every state program is subject to the same auditing standards.

(12) All this suggests we will have trouble finding ESF pertinence in WIA operation. However, there is one common concern that may offer opportunity for exchange. For WIA as for the ESF, there is considerable concern about incentives for performance. It

is one thing to spend money in ways that satisfy the auditors. It is another to spend funds efficiently and productively. WIA attempts to encourage productivity with a “High Performance Bonus” (HPB)—additional funding earned through achievement. It is American experience with this and other such incentive programs that may prove useful in planning the next ESF round.

The WIA High Performance Bonus

(13) High performance bonuses have operated since the inception of the WIA system. States can receive bonuses for amounts between $750,000 and $3,000,000 per year, depending on fund availability, if they meet the WIA HPB criteria. The potential bonuses are of the same amount, regardless of the size of the state, so each year’s award depends on the amount of funding allocated and the number of qualifying states. To receive a HPB, a state must achieve at least 80 percent of the annual negotiated target for each of the 17 WIA performance measures that are specified by statute. They must also achieve an average of at least 100 percent of the negotiated performance targets for the major performance measures groupings for adult, dislocated worker, youth, and customer satisfaction measures. These restrictions plus others connected to related programs have in all years limited bonuses to less than half of states and in recent years fewer than a dozen have been eligible.

(14) WIA law authorizes the states to use their incentive grant award to carry out innovative programs consistent with the requirements of a broad range of programs related to human capital development, and the money can be allocated to multiple purposes. States find the bonuses attractive both because of recognition accorded such achievement and because the flexibility granted for bonus expenditure permits expenditure for special projects that may not otherwise be implemented due to budget limitations. Involvement of political authorities—the governor’s office, state legislatures—in making decisions regarding bonus allocation varies from state to state. At least during the early years, the important feature seems to be the greater degree of freedom provided compared to restrictions on use of the formula-provided WIA funds.

(15) That said, financial support for the HPB has declined substantially since the program’s inception, and in recent years the entire funding allocation has come not from the Department of Labor but from the Department of Education. There program has received significant criticism from analysts both within and outside of the Department of Labor. Here are major issues:

The amounts are too low

(16) Total bonus funding amounts to $10 million on a base of $3 billion expenditure. Even with flexibility, for the larger states the potential prizes rarely exceed $1 million. In practice, this means it is difficult to pass money on down to the local one-stop operators as a meaningful addition to incentives. Given that the bonuses are determined without regard to state size, it is clear that small states are advantaged, but it is not obvious why this is desirable. Of course in government—and even, no doubt, in the EU (!)—funding is always inadequate. But without more thought about the objectives of the bonus and the tradeoffs between formula and grant funding, it is not clear what a better mix might be.

The target determination procedure is inadequate

(17) In WIA's predecessor program, the Job Training and Partnership Act, targets were adjusted on the basis of regression analysis of sources of cross-state variation in program outcomes. WIA abandoned this procedure but provided no good alternative for appropriately calibrating expectations for state accomplishment given the nature of the state's WIA client population and characteristics of state economies. Moreover, it appears the competence of the federal officials responsible for negotiating performance targets varies substantially across regions, and some state labor force agencies are much more accomplished at analytic justification for proposed targets than are others. Thus, in practice, a system intended to level the playing field seems to have made it uneven, with the results that bonuses were disproportionately achieved in some regions and a few states have garnered an exceptional number of awards without seeing targets changed.

The award system encouraged counterproductive strategic behavior

(18) Given procedures for calculating performance measures such as the rate at which participants enter employment and average earnings change, local and state performance outcomes could be improved by making determinations about who is formally enrolled in the program and how and when enrollees are recorded as having exited. For example, formal enrollment can be delayed until workers are placed in jobs or become employed. Exiting workers out of the program can be accelerated or delayed to maximize performance outcomes within a particular time period. And recall that state workforce agencies determine which workers receive intensive and training services and the mix of services those selected receive. Hence "creaming"—serving persons most likely to succeed rather than most in need of help—occurs.

There is an excessive lag between activity and reward

(19) Most would agree that the quality of data available for studying workforce policy outcomes has significantly improved since 1998, and WIA-fostered development of common measures across states should be admired by those working with EU statistics. But from a management standpoint, there remains a significant lag between the time at which productive activity occurs and the results show up in available data. Presumably the most effective bonuses are those received at a time close to when activity on which the bonus is based occurs. WIA awards accrue for achievements two years in the past. This renders the data of little use for program management or motivation.

Improvement is not incorporated

(20) Ultimately, the point of bonuses is to improve performance, and one of the objectives of the administering level of government is to translate exceptional achievement into lessons for the laggards. In addition, good government generally involves developing a culture of improvement in operation of systems. WIA failed miserably on both fronts. It appears that no systematic effort has ever been expended on determining what, if any, management techniques produced bonus-winning achievement in some states but not in others. At the same time, and at least through the eight years of the last government, little was done to modify the operation of the bonus system to improve outcomes. In part, this latter problem is a manifestation of funding issues. The WIA program was enacted for five years and expired in 2003. Since that time the program has been continued by the Congress through the appropriation process. Unsuccessful proposals to

reauthorize the program were introduced in 2003, 2005, and 2007. The program seems unlikely to be reauthorized until at least 2011. This process has discouraged restructuring.

WIA from an ESF Perspective

(21) Let me now bring up a feature of the Lisbon process that I have yet to mention: The Open Method of Coordination. The OMC was formulated and is still seen as an important tool in implementation of the European Employment Strategy and the Social Inclusion Strategy. The OMC describes a process whereby MS have committed themselves to work in a framework of jointly defined objectives, targets, and indicators, and to carry out this collaboration in the absence of a full EU legal framework for these activities. I must admit I am overwhelmed by the literature on the OMC, which has become an obsession of scholars if not, apparently, for the European public. I am aware that the OMC in practice often fails to live up to the ideal, but for students of governance, that should be no surprise. The question is how to nudge things in the right direction.

(22) The OMC dream does help identify a shortcoming of American federalism that is clearly evident in WIA. Those negotiations between states and regional DOL offices are bilateral and anything but "open." While there exist cross-state organizations—the National Governors Association, the National Council of State Legislatures, and so on—these organizations seem in many instances to be organized principally to facilitate the confrontation between states and the federal government, not for partnership across states, and certainly not for partnership with Washington in improving governance. There is much coordination to be done, and a collective approach to improving the operation of WIA and mutual monitoring should be an architectural priority for WIA authorization, if that ever occurs. I would begin with a review of what has happened with OMC with an eye for ideas for a new approach to collaboration in workforce systems development.

(23) On the ESF side, the background document "Shaping the Future of the ESF" speaks of three scenarios for ESF funding post 2013. One more or less continues current procedures. As I understand it, a second scenario calls for negotiation of outputs for each MS proposal and then linking payments to achieving these targets. The third looks to a more unified budget for MS activities, with MS responsibility for reporting achievement relative to goals for individual projects. In at least scenarios 2 and 3 negotiation of goals sounds like WIA but will be even more complicated given the diversity of ESF projects and the heterogeneity of MS management information systems. The most relevant implication of WIA experience is that target negotiation deserves careful thought and that it may be productive to offset whatever regulatory burden is created by such negotiation and monitoring with a second, "bonus' tier of more flexible funding.

Postscript: Recent Developments

(24) It would be unfair not to acknowledge that policy is changing under the Obama administration. Two developments are particularly relevant. The first is that the proposed 2011 DOL budget sets aside a small amount ($261 million) to establish two innovation funds that will "support and test promising approaches to training, breaking down program silos, building evidence about effective practices, and investing in what

works." One is for youth programs, the other is for general workforce issues. Admittedly, given the scale of WIA, $261 million does seem to bring us back to "chicken feed," but it does possibly signal a renewed commitment by DOL to making the system better.

(25) The second development is possibly more interesting. The week before the conference for which the present note was prepared, the DOL Employment and Training Administration announced a pilot demonstration in nine states to trial regression adjustment of state and local workforce board performance targets for economic and demographic variation in a manner similar to that employed over the past two years for setting national performance measure targets. According to the announcement:

> Controls for external factors 'level the playing field' across states and local workforce areas by making the targets neutral with respect to who is served and local labor market conditions. . . By adjusting or controlling for the characteristics of participants swerved at the state and local levels, the regression-adjusted targets encourage workforce system providers to more extensively serve populations with significant barriers to employment. Such an approach is consistent with ETA's planning guidance emphasis on the importance of serving low-skilled and low-income individuals. (U.S. Department of Labor, Training and Employment Notice 48-09, page 2.)

(26) This effort is led by a respected labor policy think-tank, the Upjohn Institute, operating under DOL contract. The pilot phase is intended to produce feedback from the participating states and their local Workforce Investment Boards "on ways to improve and refine the model and performance management systems." Full roll-out of the post-pilot version of the model is anticipated for program year 2011, which begins July of that (next) year. This development could have a major effect on operation of the WIA HPB, if the HPB is continued. Those considering negotiated MS goals for the next seven years of ESF funding should pay attention to these developments.