SB
50

COMMITTEE REPORT

HOUSE

4/7/81

(5)

FURTHER: JUDICIARY
(Added 4/21/81)

Date: _____

Mr. Speaker:

The Committee on LABOR & COMMERCE has had CSSB 50(L&C)

"An Act relating to unemployment insurance; and providing for an effective date."

under consideration and reports it back as follows:

[ ] do pass [ ] do not pass

[ ] do pass with attached amendments(s)

[ ] replace with CS for _____ [ ] same title [ ] new title

and recommends _____

[ ] AND attaches a "Letter of Intent" [ ] New Fiscal Note

[ ] reports it back without recommendation

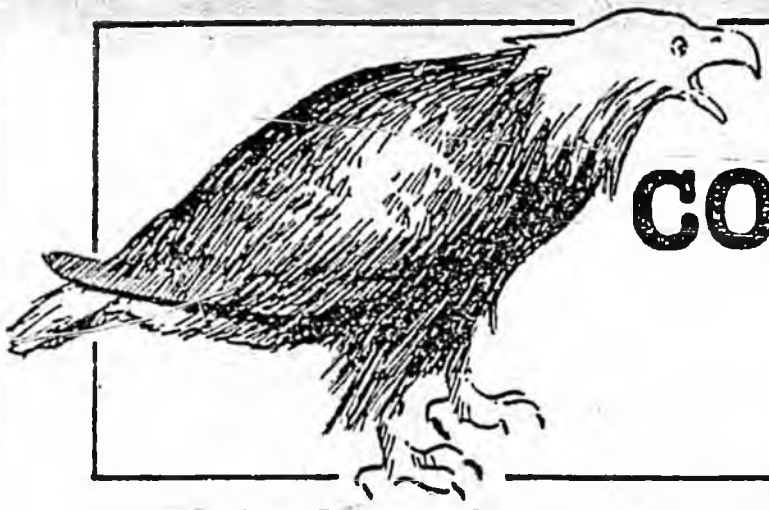
[ ] referred to the _____ Committee

MEMBERS SIGNING
DO PASS

MEMBERS HAVING
OTHER RECOMMENDATIONS:

_____
CHAIRMAN

H 60 (Rev. 3/81)



ISSUES & COMMENTARY

ALASKA DEPARTMENT OF LABOR, RESEARCH AND ANALYSIS SECTION APRIL 1981

SHOULD ALASKA OPT OUT OF THE FEDERAL/STATE UNEMPLOYMENT INSURANCE SYSTEM?

By Scott T. Hannigan

The Social Security Act of 1935 established an Unemployment Insurance (UI) program in the United States under joint federal/state management. The major role of the federal partner was administration of a uniform employer tax to fund the program. States were encouraged by the Act to pass local UI legislation with the reserved right to set qualifications and standards for the payment of unemployment compensation. The Act contained provisions for employers to receive credit against the federal tax for contributions to a state UI plan and for states to receive grants to administer their programs. The availability of employer tax credits and state administrative grants were made contingent upon states' compliance with certain features in the Social Security Act. These features were generally found acceptable to the states and a nationwide federal/state UI program was in full effect by 1937. Over the ensuing years, however, numerous amendments to the Act and additional UI legislation by Congress (requiring conforming state legislation) has led to conflicts in the federal/state partnership. The federal government has generally held the upper hand in these conflicts by virtue of the enormous financial clout provided by the tax credits and administrative grants provisions of the Social Security Act. This paper will review the historical beginnings of the federal/state UI program, some of the conformity issues facing the states, and the possibility of future changes including complete separation of the federal and state systems.

Prior to 1935, states had no programs to provide assistance to the unemployed, with the notable exception of Wisconsin, which legislated a comprehensive UI law in 1934. The major obstacle to enactment of UI laws at the state level was directly related to taxes. Specifically, it was felt that a new tax burden on employers would have a detrimental effect on interstate competition. Congress eliminated this obstacle by passing (as part of the Social Security Act) Title IX, which levied a uniform tax on all employers in the country. Title IX allowed employers a 90 percent credit against the tax if they contributed to an approved state UI program. The remaining ten percent of the tax assessment was returned to the states in the form of administrative grants. These financial incentives in Title IX plus the deepening crisis of the 1930's depression strongly encouraged enactment of state UI laws and all states had unemployment insurance programs in operation by 1937. Provisions of Title IX were removed from the Social Security Act and were placed in the Internal Revenue Code by the Federal Unemployment Tax Act of 1939 (FUTA).

Original proponents of the Social Security Act vigorously debated the type of UI program to be recommended--a wholly federal system or a federal/state plan. Arguments for a national system included, among others, that a national system would provide uniform protection from the risks of unemployment, protect the interests of multi-state employers and workers, provide for a national pooling of reserves, and streamline reporting requirements and the payment of taxes. Those who favored a federal/state program argued that a national system would be cumbersome to operate, that centralization would tend to paralyze action, that controversial issues would not receive proper debate and discussion by the states, and that a federal/state system would allow states to tailor the program to fit their needs and would allow wide latitude for experimentation by the states and so aid in producing a better system.[1/] The federal/state plan was the one that finally emerged.

The issues of conformity have existed since the very start of the unemployment insurance program. The Social Security Act contained several provisions that the states were to comply with. Titles III and IX of the Act required state UI laws to include the following major provisions: (1) payment of UI benefits solely through public employment offices or other approved agencies, (2) opportunity for a fair hearing on denied claims, (3) payment of all tax monies collected to the U.S. Treasury (Unemployment Trust Fund), (4) expenditure of all money requisitioned from the Trust Fund for UI benefits only, (5) no benefits to be paid until two years after commencement of tax collections, and (6) several provisions protecting conditions of work acceptance by claimants. Other provisions refer to administrative and reporting requirements. To enforce state conformity to these provisions, the Social Security Act allows for the denial of all employer tax credits and the suspension of state administrative grants. On numerous occasions since the inception of unemployment insurance, Congress has passed amendments to the Act necessitating conforming legislation at the state level. A major example has been amendments that have extensively increased UI coverage to such worker groups as state and local government employees and employees of non-profit institutes.

More recent conformity issues have included pension offset provisions (P.L. 96-364) and provisions of the 1980 Omnibus Reconciliation Act (P.L. 96-499). The pension offset provision requires a reduction of a claimant's weekly benefit by the amount of any pension (attributable to a base period employer) received by the claimant. The Reconciliation Act requires conforming state legislation to deny the payment of extended benefits for voluntary quits and discharges for misconduct regardless of applicable state law for regular benefits (i.e., if state law reinstates benefit entitlement for regular benefits after a penalty period, the entitlement would be cancelled for extended benefits). Failure to accept suitable work (as defined by federal law) or failure to seek work also results in denial of extended benefits.

Even further encroachment by the federal government will occur if recent proposals of the Reagan Administration are adopted. These include (1) changes in the extended benefits program to eliminate the national trigger and to revise the methods of calculating state triggers (both of which determine when extended benefits are to be paid); (2) requirements that unemployed workers who have collected 13 weeks of state UI accept any job that meets minimum wage and safety standards if the wages are equal to or greater than their UI benefits; and (3) eliminate UI for those who leave the military voluntarily.

The rising spectre of federalism in unemployment insurance has caused concern in

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1/ William Haber and Merril G. Murray, Unemployment Insurance in the American Economy, Richard D. Irwin, Inc. 1966.

Alaska and many other states. In most conformity issues, the states have grudgingly complied with federal legislation because they fear to lose tax credits for their employers and administrative grants for their programs. The mere threat of sanctions has kept states in line and the sanctions have never been fully applied. A specific instance where Alaska has run headlong against the federal government has been on the issue of interstate benefits. In 1955 and again 1960 Alaska reduced the maximum weekly benefit amount to out-of-state claimants in order to curtail the amount of UI dollars leaving the state.* The state was required to retreat from this position in 1972 when Congress decided the practice was discriminatory to the rights of workers to move from state to state seeking employment. This interstate question has become a point of concern in recent years as Alaska has seen one-third of all its UI dollars pouring out of the state, aiding the economies of other states instead of our own. An even larger problem looms in the future amid talk of federal benefit standards requiring a maximum benefit equal to 2/3 of a state's average weekly wages. Alaska traditionally pays more benefits per dollar of total wages than any other state. This standard would put employer costs through the ceiling and could possibly drain the state's trust fund.

Potential solutions to the partnership problem are varied and complex. Many people over the years have advocated complete federalization of unemployment insurance. Most states, however, take a dim view of this type of encroachment on their rights. Another course would be to maintain the present system with some sort of systematic court review of conformity sanctions.[2/] The most extreme solution would be for a state to permanently refuse to comply with federal legislation.

The remainder of this paper discusses ramifications if Alaska chooses to remove itself from the federal/state system. The most direct effect would be monetary. Shown below are cost estimates for Alaska's UI program in 1982 comparing an out of conformity situation with a conforming one.

	Estimated Costs for 1982	
	In Conformity	Out of Conformity
State Taxes	$63.6 million	$63.6 million
FUTA Taxes	7.0 million	34.0 million
UI Administration	Federal Grants (From FUTA Taxes)	11.5 million
ES Administration	Federal Grants (From FUTA Taxes)	7.9 million
Extended Benefits (50% Federal)	Federal Reimbursements (From FUTA Taxes)	4.5 million
TOTAL	$70.6 million	$121.5 million

*Ch. 5, ESLA 1955 and Ch. 60, SLA 1960.

2/ Ibid.

The comparison shows that operating the current program while failing to conform to federal requirements would result in additional costs of $50.9 million. Most of the cost ($27 million) would be levied on employers as a result of lost FUTA tax credits. Employers might also be expected to pay administrative costs as well as funding full benefit outlays. If that were the case, employer costs would increase by approximately seventy percent. This burden could be reduced if employee contributions were increased and/or the state absorbed administrative costs.

One major question of the conformity issue concerns federal responsibility if employers opt to pay the full FUTA tax. The system was designed to pay benefits equal to 2.7 percent of taxable wages. Of the three percent FUTA tax, this 2.7 percent was to be dropped if employers contributed to the benefit fund of an approved state program. The implication is clearly that the 2.7 percent was to be used for paying benefits. Further, if employers opt to pay the full FUTA tax, the implication is that no state taxes would be necessary because the federal partner should be responsible for benefits.

The system was not--at least, should not have been--designed to coerce states into setting up their own unemployment insurance programs. Since costs would be three percent of taxable wages under a state or federal system, states would obviously find it attractive to design systems to fit their own social and economic conditions rather than accept standards determined in Washington. This "logical interpretation" does not coincide with the "legal interpretation." According to an unofficial opinion of the Solicitor General, the federal government has no power to implement an unemployment insurance program in any state. In other words, the system was designed to force states to implement unemployment insurance programs via making them pay for one whether they have one or not.

Failure to maintain an approved program would result in the 2.7 percent "credit" flowing into the federal administrative account rather than a benefit account, with the state receiving no funds in return. No state has informed the federal partner that it intends to drop its own program in favor of federalization and so the position remains unchallenged. It is conceivable that the "back door" federalization now in progress will change this situation in the future. The issue is not a simple one and raises a host of questions about the federal/state relationship. Some alternative relationships that might be considered for the operation of an unemployment insurance program in Alaska are discussed below.

The discussion centers on estimates of the average employer cost per worker (with annual earnings at or above the taxable wage base of $13,[illegible]) and includes the current system for comparison purposes.

CURRENT SYSTEM		
FUTA Tax (0.7% of first $6,000)†	=	$ 42
State Tax (3.3% of first $13,300)	=	439
TOTAL TAX	=	$481

One (untested) alternative is to drop the state system in favor of a federal program funded from the maximum FUTA tax. Employers would then pay the full FUTA tax of $204 per employee and all program provisions would be determined in Washington.

FEDERAL SYSTEM		
FUTA Tax (3.4% of first $6,000)†	=	$204
TOTAL TAX	=	$204

A second alternative would supplement a federal system with a separate state system. Costs would be dependent on the level of benefits the state wishes to provide. The state system would also require administrative funds of approximately $19 million.

An independent state program is a third alternative. The cost figures below assume that the full FUTA tax is paid and that the state receives no funds in return. Obviously the combined cost of running a state system and paying penalty FUTA taxes could exceed the capabilities of many employers to pay. Some form of state assistance may be necessary (especially in light of expected increases in the taxable wage base for FUTA which will probably become effective in 1983 or 1984). The most plausible forms of state assistance are assumption of the liability for FUTA taxes and/or administrative costs and state support of benefits through appropriations to the UI Trust Fund.

INDEPENDENT STATE SYSTEM		
State Tax (3.3% of first $13,300)	=	$439
FUTA Tax (3.4% of first $6,000)	=	$204
Administrative Costs		$120
TOTAL TAX	=	$703

There are a number of areas where Alaska could effect some cost savings if the state were running an independent UI program. Some cost saving areas and approximate dollar amounts are listed below:

†The FUTA tax is set at 3.0 percent of the first $6,000 of each employees wages. The rate was temporarily increased to 3.4% to reduce the national debt in the FUTA account. If a state's UI law is in conformity with federal law, then employers receive a 90 percent credit on their FUTA taxes and pay in effect 0.7 percent (10% of 3.0% = 0.3 + 0.4 added tax = 0.7%).

Discussion of opting out is often the result of frustration with the expanding role of the federal partner and of a realization that this expansion cannot be successfully countered by piecemeal resistance to individual intrusions on state prerogatives.

Before taking a radical step, alternatives should be considered. The level of interference by the federal partner has increased substantially since the unemployment insurance trust funds were placed in the federal unified budget in 1969. In attempts to reduce budget deficits, Congress has enacted several changes to the UI system. Although the changes may have been proposed primarily for their budgetary effect, they have had profound impact on the program and on the nature of the federal/state cooperative arrangement. The key to a return to true partnership may lie in removal of state trust funds from the federal unified budget. Alleviating budgetary pressure may accomplish many of the desirable goals of opting out without some of the negative aspects. That is, removal of the trust funds from the budget could reverse the tendency toward federal intervention and would not carry the potential to destroy the existing federal/state partnership.

Briefing Paper: CSSB50
Conformity Amendments to Unemployment Insurance Law (AS 23.20)
April 28, 1981

Replacing current law with a benefit schedule that pays no extended benefits but pays 32 weeks of regular benefits is expected to cost about $16 million in 1982. Claimants would receive approximately $6 million of this additional cost. The cost analysis is easier understood if broken into three parts. These are explained in the following discussion and summarized in the table below.

Eliminating variable duration and adopting a fixed 26 week duration would give an additional $12.1 million to claimants. Naturally, employers must pay this cost, but additional costs would be incurred when some claimants shift from extended benefits (for which the state and feds pays equal shares) to regular weeks (for which the state pays the full amount). This cost would be approximately $2.7 million in 1982 and brings employer costs to $14.8 million.

In going from a 26 week program (still paying EB) to the 32 week proposal with no EB, benefit amounts would be unaffected but contributions would have to be increased to cover the federal share of weeks 27 through 32. This amounts to half of the $8.2 million payable to that group, or $4.1 million. Elimination of weeks 33 through 39 would save the trust fund $3 million, but claimants would lose $6 million of combined state and federal funds.

Effect of Replacing Current Law with a Program
Paying 32 Weeks of Regular Benefits and No EB
(Estimates for 1982)

	Employer Cost/(Savings)	Claimant Gain/(loss)
Elimination of variable duration	$14.8 million	$12.1 million
Federal share of weeks 27-32	4.1	0
Nonpayment of weeks 33-39	(3.0)	(6.0)
TOTAL	$15.9 million	$ 6.1 million

In considering this proposal, several other points should be discussed. Some of these are listed below.

1. The work search and acceptance requirements in CSSB50 are federal conformity issues. Alaska will be out of conformity if we fail to pass all of CSSB50, even if Alaska adopts a 32 week program and does not pay extended benefits. Whether we are out of conformity by a little or a lot makes no difference -- the penalty is the same. The impact of failure to conform is massive and was communicated in the latest "Issues and Commentary".

2. There are three variables which affect benefit outlays in the unemployment insurance program -- benefit amount, duration of benefits, and eligiblility. These variables were balanced in the law adopted last year and altering only one of the three will throw the system out of balance.

3. Interstate benefits would be payable for 32 weeks rather than the 21 week average payable (under the revisions included in CSSB50) to claimants in states not triggered on to the extended benefits program. This factor is not included in the estimates above, and would add about $1 million to costs.

4. The 32 week proposal would reduce potential duration for the 42 percent of claimants who presently qualify for more than 32 weeks.

5. With duration fixed at 32 weeks and no EB, people with strong attachment to the labor force would get 7 weeks less entitlement than today while claimants with very weak attachment would get 8 weeks longer duration than today. Some claimants could be entitled to more than they earned: e.g. claimants with earning of $1,000 would be entitled to ($34 x 32 =) $1,088 instead of $816 ($34 x 24) as today.

6. Coupled with the current benefit schedule, fixed duration provides a disincentive to work, particularly for claimants with weak attachment to the labor force. This increases the potential for abuse and causes additional costs which are hard to measure and have been omitted from the estimates.

Alaska State Legislature

Senate

Judiciary Committee

Official Business

Pouch V
State Capitol
Juneau, Alaska 99811

April 20, 1981

Mr. John Quinn
Naval Security Group
Adak, Alaska 99695

Dear John:

Thank you for your comments on CSSB 50.

The bill was not referred to the Judiciary Committee before it passed the Senate. The bill is now in the House Labor and Commerce Committee, chaired by Representative Hurlbert. I have taken the liberty of forwarding a copy of your remarkes to him for his information.

I appreciate your thoughts on the matter.

Sincerely,

Senator Patrick M. Rodey
Chairman

cc: Representative Hurlbert, Chairman
House Labor & Commerce Committee

April 12 Th

NAVAL SECURITY GROUP ACTIVITY
ADAK ALASKA
WESTERNMOST LINK

NAVAL SECURITY GROUP
ADAK, ALASKA

RECEIVED
APR 16 1981

Dear Pat

I would like to know if CSSB50 which you opposed has been put through the judiciary committee to determine the bills constitutionality. It is very logical that a person would move to a state with very low unemployment inorder to seek meaningful work. Under this bill if I relocate to a high unemployment state, then I can be eligible for benefits. I would like to hear from you and wish your associates in the House will see the contradiction in the Bill outlined above.

Best Wishes
John Quinn

Bill No. Senate Joint Resolution No.

Date April 20, 198[illegible]

Title Relating to exclusion of state unemployment insurance trust funds from the federal unified budget.

Contact: Judy Knight JK
465-2700

Funds used for unemployment compensation are generated by payroll taxes enacted by State Legislatures. These funds can be used only to pay unemployment compensation in the state in which they were collected and are held in trust by the federal government and drawn as needed to pay benefits. Since 1969, these funds have been included in the unified budget. The "bottom line" impact of inclusion of state trust funds in the unified budget is that all unemployment compensation--including benefits paid completely from dedicated state funds--appear as federal outlays. This makes unemployment insurance programs the target for budget-balancing proposals such as taxation of benefits, pension offsets, removal of extended benefit claimants from the computation of unemployment rates, and other cost-cutting proposals like those included in the Omnibus Reconciliation Act of December 5, 1980.

In addition to those set out in the Resolution itself, there are a number of other reasons unemployment compensation trust funds should not be included in the unified budget, as follows:

1. The majority of the federal payroll tax is not collected from employers, but is credited if employers participate in an approved state program and are subject to contribution rates set by the state.

2. The operations of the U.S. Treasury do not require that the accounts be included in the unified budget. The Treasury currently handles accounts for several "off-budget" agencies.

3. Basic program decisions--level and duration of benefits, contribution mechanisms, eligibility, and many administrative functions--are almost entirely in the hands of state legislators.

Policy calling for removal of funds has been adopted by the National Governors' Association, the Interstate Conference of Employment Security Agencies, the Federal Advisory Council on Unemployment Insurance, and the National Commission on Unemployment Compensation. These policy positions were adopted recently and the issue is not yet well-known in Congress. One way to speed consideration of this important issue is to ensure that states' Congressional delegations recognize the impact of inclusion of state unemployment trust funds in the unified budget and are aware of the states' strong desire to remove the funds from the budget. The proposed resolution could be used to convey Alaska's sentiment on this issue to rational policy-makers.

Position: The Department of Labor supports the proposed resolution and recommends immediate approval.

POSITION PAPER/Department of Labor

COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 50
SECTION BY SECTION ANALYSIS

Section 1: AS 23.20.362

This section repeals and re-enacts AS 23.20.362 with the following changes:

1) The pension deduction provision required by Sec 3304(a)(15), FUTA, is amended to conform with Public Law 96-364. Under this amendment, a pension would be deductible from benefits otherwise due only if the pension is provided under a plan maintained or contributed to by a base period employer, and the claimant's service in his base period increased the amount of, or affected his eligibility for, the pension or other retirement pay. In addition, that portion of the pension attributable to the claimant's own contributions will not be deducted from his benefit amount. Public Law 96-364 does not require these changes to state pension deduction provisions; rather, it allows the state this option of liberalizing the required provisions. However, the changes are equitable and would benefit Alaskan workers. For example, the previous provision required a 100% deduction even if part or all of the pension was based on employee contributions. This, in effect, penalized individuals for saving some of their wages by deducting amounts which had actually been earned long before the unemployment insurance claim was filed.

2) The proposed amendment also distinguishes between pension payments and payments received for dismissal pay, accrued vacation and sick leave, or holidays. The previous provision had the effect of prohibiting deductions for dismissal pay, vacation pay, or holiday pay unless the week <u>began</u> in a period for which such payment was made. The proposed amendment provides simply that any such payment attributable to a week will be deducted from benefits payable for that week. Sick leave has been added to the list of deductible payments. The rationale for deducting vacation pay, holidays, etc., applies to sick leave as well.

Section 2: AS 23.20.375(b)

This section repeals and re-enacts AS 23.20.375(b) to require a waiting week on all claims. The current provision waives the waiting week requirement on transitional claims. However, Public Law 96-499 now requires that any state which provides for payment "(at any time or under any circumstances) of regular compensation to an individual for his first week of otherwise compensable employment" will not be reimbursed for the federal share of the first week of extended benefits paid in the state. This requirement is not a standard for certification of state laws. The requirement must be met, however, if the state is to receive the 50% reimbursement of the federal share of the first week of extended benefits. This amendment conforms to Public Law 96-499.

Section 3: AS 23.20.390(b)

This section makes <u>both</u> "good faith" and "hardship" a requirement for waiver

of overpayments. The current provision allows an individual who has not acted in good faith to nevertheless be absolved from liability for repayment if he can show that great hardship would result from charging him with repayment.

Section 4: AS 23.20.406

This section amends AS 23.20.406 by adding new eligibi requirements for receipt of extended benefits. These requirements are c formity standards established by Public Law 96-499 and must be included in a state's law for weeks beginning after March 31, 1981, in order for the law to be certified by the Secretary of Labor on October 31, 1981, and thereafter.

The amendments require the following:

1) Denial of extended benefits to an individual who has been disqualified for regular UI benefits for voluntary quit, discharge for misconduct, or job refusal, unless the disqualification was terminated by subsequent employment.

2) Denial of extended benefits to an individual who does not actively seek, apply for, or accept suitable work when referred to such work. Suitable work is specifically defined in the provisions. The disqualification can be terminated only by new employment of at least four weeks and earnings of four times the weekly benefit amount.

Section 5: AS 23.20.408

This section amends AS 23.20.408 to specify that only the first two weeks of extended benefits are payable to an individual who files on an interstate basis from a state in which an extended benefit period is not in effect. This change is required, for certification of all state laws, by Public Law 96-364.

This amendment was requested by Alaska and introduced by Senator Stevens. House Joint Resolution No. 59 passed by Alaska's Legislature last year supported this change.

The provisions of Sections 1, 2, 4, and 5 are conformity issues to comply with federal law.