REVITALIZING UNEMPLOYMENT INSURANCE

By The Secretaries' Innovation Group

By:

SIG Subgroup of Workforce Secretaries

Draft October 2015

NOTE REGARDING THIS UPDATE

Since the time we published the SIG proposal for Unemployment Insurance, we have engaged in conversations with members resulting in suggestions which we have incorporated into this draft. In particular, we have responded to the comments made by several members expressing frustration with the inflexibility of the current system and suggesting that SIG produce in this revision additional options short of our full-scale proposal in this revision.

By Larry Temple and Curt Eysink

OVERVIEW: THE FEDERAL-STATE UNEMPLOYMENT INSURANCE SYSTEM

The basic structure of the UI system has been set in law since 1935. The structure of the system, though, has seen little to no change in the nearly 80 years it has existed and it's time that changed.

The current unemployment circumstances call for a re-evaluation of the basic UI structure. We can learn lessons from other programs. Unlike UI, a similar payroll-based program in the US, the workers' compensation system (WC), has evolved over time because it incorporates flexibility for states to utilize various industry and regulatory structures. Workers' Compensation program evolution is just one example. Welfare significantly benefitted from experimentation - - before the federal welfare reform law fundamentally changed the system in 1996, a number of states had secured waivers to change their programs. The most successful state experiments were later embodied in federal law and drove significant improvements in recipient individual and family outcomes. In short, the experience of varying state programs helped the entire country find a better way to help those on welfare move to employment and self-sufficiency.

Recrafting the UI system to offer states more flexibility would involve allowing states to offer innovative methods to find jobs for the short-term and long-term unemployed while preserving benefits to support them in the meantime. These options could include:

- Greater efforts at work activation through hands-on assessment, job development and re-employment.

- Explicit reorientation of federal goals toward job placement over speed of benefit application processing.

- Innovations with reimbursing/self -insurance and with alternative private insurance options with elements similar to workers' compensation.

FOUR BIG DEMONSTRATION OPTIONS TO GET POLICY CHANGES MOVING IN THE RIGHT DIRECTION

The Secretaries' Innovation Group proposes that the Congress enact legislation that could permit a four (or more) demonstration options, from the most comprehensive state-owned system, to important but subsidiary concepts. Each of the four options presented below are state opt-in. Interested states would choose their demonstration option from among the four, and up to a maximum of seven states would be permitted to opt-in to each option. This would yield a maximum total of 28 potential simultaneous demonstrations (maximum of seven states times four options).

Option One. States to own and manage their own statewide UI system

In the most comprehensive of the four proposed options, States would *create and manage their own statewide unemployment insurance system* consistent with proper purpose and protections. Such a program would be designed so as to be solvent over the long term and sufficiently funded to provide adequate insurance protection for the unemployed.

General Features under Option One

- The state owned system would retain the options currently available under the federal program, including determining level of benefits, maximum duration, and the obligations of workers to seek employment. States would have broad new authorities to determine the nature of the program and how it is funded, with some of the options as described below.

- A small portion of the current FUTA tax sufficient revenue would be allocated sufficient for Federal administrative purposes only. Remaining FUTA funds and all SUTA funds would be placed in state owned and managed trust funds.

- States would have the authority to fund the state trust fund as now through payroll taxes, and may use alternative or supplementary mechanisms.

- All recipients of unemployment benefits at the date of the change-over would remain in the existing program. New initial applicants would be covered under the new arrangement.

- States would retain the option of participating in special Federal funded extensions during periods of high unemployment under the same terms as states which have not opted in and remain in the Federal system.

- State UI loan balances owed to the Federal government would remain obligations as they are now.

Option Two. Expand reimbursing option any employer within the state

This option would *permit contributing employers to elect to be reimbursing employers* under the same basic terms as under current law for non-profits and certain other entities. Once an employer elects to be a reimbursing employer, such designation could not be reversed for five years (to prevent gaming). The state would measure outcomes of the demonstration, including reports showing (a) the number of employers electing the option; (b) the duration of unemployment compensation of individuals who became unemployed; (c) the reemployment rate of individuals who became unemployed from pilot employer entities; (d) the average duration and reemployment rates of reimbursing vs. contributing employers in the state.

Option Three. Permit employers to purchase private UI insurance as an alternative to state UI plan.

State *would permit employers to purchase a five to seven year private insurance policy for their employees* as an alternative to public insurance. In order to elect private market coverage the employer would be required to have a positive balance in its state unemployment insurance account equal to 1.0 times the average high cost, and maintain records sufficient to enable the state to calculate a contribution rate for the year after the conclusion of the pilot. The insurance policy would be regulated by the state entity that regulates workers' compensation plans.

Option Four. Dedicated set aside of small portion of SUTA tax for targeted efforts

States could *set aside up to 2% of its state unemployment tax revenue* for use in administration of Reemployment Eligibility Assessments and Reemployment Services of claimants who are unemployed and not expecting to return to their job, as defined here:

1) do not receive job referral through hiring halls established under collective bargaining agreements;
2) have not received a specific return to work date from an employer; and
3) are totally unemployed (i.e. not partially unemployed due to part time work, etc.).

The 2% funds could be used to pay for administrative costs associated with initiatives that reduce the duration of benefits, increase reemployment and reduce overpayments. Examples of interventions include targeted reemployment services, improved identification of fraud, and efficient collection of overpayments. Administrative funding would not be subject to "merit staffing" requirements of Section 303 of the Social Security Act.

Problems with the Current Federal UI System

UI has become an inflexible system. Federal restrictions constrain the ability of states to manage their programs so as to maximize the return to work of the unemployed.

Funding constraints. For example, federal law requires, as a condition of qualifying for reduced federal tax rates, that states place their unemployment tax collections for benefits (SUTA) into a federal unemployment trust fund within the federal unified budget. The return on these funds is typically well below market return. Federal payroll taxes collected for the fund (FUTA) can only be used for federally specified purposes and, with limited exceptions, may not be combined with state SUTA funds to help speed back to work efforts.

Emergency expenditures. In recessions, lawmakers often add a federal "emergency" extended benefit program (EUC) that includes inflexible rules about where, when, and for how many weeks federal unemployment benefits are paid out. The permanent federal extended benefit program (EB) reimburses states for 50% of extended benefit expenditures, with federal law specifying when federal funds can be used. As a result, states (and employers in the state) have limited control over the timing or duration of such measures, or discretion in putting these often significant funds to better use to assist the unemployed.

One-Size-Fits-All insurance. Alternatives that could lower unemployment taxes to employers, such as reimbursement/self-insurance or the use of private insurance options, are not consistent with existing federal requirements and are therefore not available under current law. Statutes and rules constraining the creative development of a thriving private supplementary or alternative UI system similar to workers' compensation that states currently operate, cannot be applied to UI.

Welfare functions. Moreover, changes to law relating to access to the special fund under the Obama stimulus funding, have required states to expand benefits and take

on some of the characteristics of public assistance (such as providing UI benefits to individuals seeking only part time work or who have quit jobs for certain reasons - - inconsistent with the UI social insurance principles. State policy decisions should be the province of the states that are responsible for the integrity and solvency of the state UI trust funds based on "insurance principles" and not public assistance.

Absence of sufficient reemployment focus. Unlike some other federal benefit programs, the federal regular UI program has no effective reemployment or engagement goals. Instead, its measures are focused primarily on UI benefit payment outcomes, e.g. payment accuracy and timeliness. As a result, claimants are less engaged in job search than they should be to land a job in a timely fashion.

Administrative resistance. Even in circumstances where states have proposed and Congress has acted specifically to authorize state flexibility to allow innovations in back-to-work solutions (e.g. PL 112-96 enacted February 2012), this effort has been discouraged through DOL administrative policy, in this instance resulting in all states declining to submit requests.

WHAT ARE CHANGES STATES MIGHT INCORPORATE UNDER A STATE-DESIGNED UI SYSTEM?

- *Active case management.* State unemployment offices which change their orientation so as to view their mission as putting people to work, as opposed to just paying out benefits, can have a sizeable impact. Texas has boosted by 50% the proportion of beneficiaries working in the tenth week after UI enrollment through a specific back to work orientation and goal measurement within its job service offices. Many states are experimenting with the federal grants for Reemployment Eligibility Assessment (REA) programs and seeing as much as a 400% return on investment in case management to help claimants return to work.

- *Temporary short-term work options.* Texas, Oregon and other states have had success offering a subsidy to employers to create new positions for unemployed individuals at the lower end of the experience and training scale, getting them working sooner. The Georgia Works program offers to trainees a stipend while undergoing eight weeks of on-the-job training with an employer.

- *Optional lump sum payments at the outset of unemployment or bonuses to workers who find new jobs quickly* The totals expended would be equal to or less than the anticipated drawdown for the duration of unemployment, based on state-designed profiles. Bonuses tested in four states were found to be effective at inducing re-employment.
- *Extend the "Reimburser" option to self-insure, to all employers*. Presently, non-profit organizations, government agencies, and Indian tribes have this option. There is no reason this provision, which reduces costs to employers and the UI system,

should not be extended to all private employers, with proper oversight and protection.

EXAMPLE - - WORKERS' COMPENSATION OFFERS AN INNOVATIVE OPTIONAL MODEL FOR UNEMPLOYMENT INSURANCE UNDER STATE UI OWNED SYSTEM.

All 50 states have workers' compensation systems, even though there is no federal law requiring this (federal employees have their own coverage). The workers' compensation system has many desirable features, notably flexibility for states to experiment with different industry and regulatory structures. The basic features of a workers' compensation state-run model could easily be adapted to a state unemployment compensation system if adopted as proposed by the Secretary's Innovation Group.

Workers' compensation is a system of insurance like UI. But it differs in important ways. First, the price of the insurance is more closely calibrated to employer experience, signaling its true costs (states also provide high risk pools so that universal coverage is always available).

Second, unlike UI, employers can secure workers' compensation coverage in flexible ways to suit their needs - either through reimbursement/self-insurance or by purchasing insurance through the state or another insurer. In WC in recent years, about 25 percent of employers have self-insured, about 18 percent have purchased insurance through the state or federal programs and the rest, 57 percent have opted for coverage through non-government insurance carriers.

Third, the institutional incentives of both parties, employer and employee, encourage return to work as soon as possible. This has become evident through the steady and substantial reduction in on-the-job injuries since the early nineties, suggesting positive employer incentives are at work. Fourth, workers' compensation often utilizes third party administrators to efficiently administer claims and settle conflicts. Fifth, the WC system commits payment errors far below the ten percent rate typical of UI.

Last, the greatest strength of the WC system is the diversity of program design inherent in the various state systems.

CONCLUSION: THE EXPECTED BENEFITS

The federally dominated UI system promises more benefits than it can deliver. A state owned and managed UI system will provide management and budget discipline. It can potentially bring in self-insurance as well as the insurance market to properly price

and deliver benefits under a better alignment of interest between taxpayers and job seekers. Finally, it can provide dozens of separately designed and operated solutions to unemployment, enlightening national policy and encouraging change.

APPENDIX

Unemployment Insurance System in a Nutshell

Federal tax When a state UI program meets all federal requirements, employers in the state pay a federal tax rate of 0.6 percent plus state UI taxes. Revenue from the federal tax is used to pay federal and state administrative costs of the UI program; the federal share of Extended Unemployment Compensation (EUC) benefits during times of high unemployment; loans to states to pay their share of UI benefits; and some labor information programs.

Reimbursers/Self Insurance. Nonprofits, governments and Indian Tribes can opt to reimburse the state for their actual costs of layoffs, instead of paying the SUTA tax.

State UI taxes are based on schedules of minimum and maximum rates on a set taxable wage base. Two states use a taxable wage base of $7,000, the minimum for employers to receive federal credits. The highest wage base is in the state of Washington at $41,300 in 2014.

- *The rate* employers pay against the taxable wage base depends on their "experience rating," a risk-based continuum that varies rates according to how much or how little their workers received unemployment benefits. Employers with a history of lay-offs may be subject to maximum rates; employers who have laid off few workers are subject to the minimum rates. State minimum rates range from zero to 2.8 percent (PA in 2014); maximum rates range from 5.4 percent to 15.4 percent (MA in 2014). New employers generally pay a fixed rate until they qualify for an experience rating schedule. The tax rates are applied to a taxable wage base, or ceiling, set by each state.

- *State surtaxes* can be imposed for purposes such as targeted fund-building, rate reductions for low turnover employers, to repay bonds or interest on federal loans, and for job training and placement programs.

Payment and Duration of Benefits. States determine a weekly benefit amount and duration of benefits. The weekly benefit amount is generally calculated as a percentage of previously earned wages during a designated period of time. In January 2015, for instance, the average weekly benefit was $315, or about 36 percent of the average weekly wage. Weekly benefits ranged from $204 in Mississippi to $445 in Hawaii. The duration of state-provided benefits has grown over time, rising from 15-16 weeks in the 1930s to generally up to 26 weeks today.

Federal Extensions of UI Benefits. Congress routinely enacts temporary programs providing special extended benefits during periods of high unemployment. In the most recent economic downturn, unemployed persons could under certain circumstances receive up to 99 weeks of benefits. These extended benefits (EUC and EB) are financed directly by Congress and

eligibility depends on each state's unemployment rate (these extensions expired at the end of 2013).

Number of Beneficiaries. In times of low unemployment, generally between 2 and 3 million individuals draw unemployment benefits at any given time; in times of elevated unemployment, it is higher. In June 2011, 3.6 million individuals were drawing state UI benefits, 3.2 million individuals were drawing EUC benefits, and 0.6 million were drawing EB program benefits, for a total of 7.5 million recipients out of an out of an estimated 14.5 million unemployed. In December 2014, 2.4 million individuals were drawing state UI benefits as EUC has ended and regular EB only triggers on at higher total unemployment rate (currently no state is triggered on EB).

MEMO TO: Celina Bussey, Chair, UI Committee
Jackie Turner, Vice Chair, Administration and Finance Committee

COPY: Ellen Golombek, President NASWA

Dennis Murphy CT
Michelle Beebe UT
Laura Boyett ME
Neil Gorrell WA
Jeff Mays IL

FROM: Jason Turner, Executive Director, Secretaries' Innovation Group
Doug Holmes, President UWC

RE: Secretaries' Innovation Group proposal discussion

DATE: July 23, 2015

Greetings Celina and Jackie - -

Thank you both for including Doug Holmes and me on the Chicago agenda, and for leading the discussion of the four state UI options. We found the meeting very productive, and your members raised some important questions for discussion which we have had time to consider with resulting improvements to the proposal.

Among the issues in the robust discussion were these:

- Laura Boyett asked if states would continue to meet federal conforming compliance rules if the state opted to own and manage its own program (SIG option 1). *The proposal would require that the Federal statute be amended so that the special treatment of the deposit and use of FUTA revenue would not raise a conformity or compliance issue and FUTA tax revenue would continue to be collected consistent with federal law. State law would define the deposit and use of these funds, respectively.*

- Jeff Mays raised the prospect that some state legislators may try to transfer the FUTA revenue (which would become state funds) to provide funding for other purposes. *State and Federal statutory language will have to be clear and tight on the permitted uses of these funds and the process for spending authorization and expenditure or appropriation.*

- Michelle Beebe asked whether the redirection of trust funds to a participating state would reduce the amount of federal funds available to the remaining states in the event of a shortfall in the federal trust fund account. *Although the FUTA funded accounts were originally designed to be the accounts into which FUTA funds were deposited and from which federal appropriations were made for administration, the appropriations process changed over time so that it does not limit the appropriations for state and federal administration to amounts in the FUTA funded accounts. To the extent that there is a deficit in the FUA or EUCA account there is an automatic transfer of federal general revenue to cover the need to pay unemployment compensation and amounts appropriated for administration at the federal and state level are not limited to amounts shown in the FUTA funded accounts. Nonparticipating states would continue to be eligible for administrative funding through the current process.*

- Neil Gorrell inquired as to whether under SIG option 2, if low user employers were to become reimbursing employers, would this make funding less available to subsidize the heavy users. *The reimbursing option is consistent with experience rating and will have the effect of improving business management of each participating employer's labor force. In addition, the state may choose to incorporate a small "social tax" which is added to the state fund and payable by all reimbursing employers to supplement the general state fund to cover any shortfall in the state trust fund that might occur.*

We look forward to continuing to work with your committees as we seek to strengthen the proposal options.

Yours truly, Jason Turner and Doug Holmes