

HOUSE BILL REPORT

2ESB 6097

As Passed House - Amended:

June 11, 2003

Title: An act relating to revising the unemployment compensation system through creating forty rate classes for determining employer contribution rates.

Brief Description: Revising the unemployment compensation system.

Sponsors: By Senators Honeyford and Mulliken.

Brief History:

Second Special Session

Floor Activity:

Passed House - Amended: 6/11/03, 52-38.

Brief Summary of Second Engrossed Bill (As Amended by House)

- Reduces the maximum weekly benefit amount to \$496 or 63 percent of the state average weekly wage, whichever is greater.
- Reduces the maximum benefit payable to the lesser of 26 times the weekly benefit amount or 1/3 of the total base year wages.
- Beginning in 2004, reduces an individual's weekly benefit amount to 3.9 percent of the average of the individual's wages in the two quarters of the base year in which wages were highest.
- Narrows the reasons for "good cause" quits and broadens the definitions of misconduct.
- Allows certain part-time workers to search for suitable part-time work.
- Creates a new tax array beginning in 2005 that has 40 rate classes and uses rates based on three factors.
- Caps the new tax rate at 6.0 percent for certain seasonal industries (fishing, agriculture, and food processing) and at 6.5 percent for other industries, except when a solvency surcharge applies.
- Requires that certain benefits are charged to the experience rating account of only the separating employer.

· Establishes penalties for certain employer delinquencies and/or misrepresentations.

HOUSE COMMITTEE ON COMMERCE & LABOR

Majority/Minority Report: None.

Staff: Jill Reinmuth (786-7134); Chris Cordes (786-7103).

Background:

The unemployment compensation system is designed and intended to provide partial wage replacement for workers who are unemployed through no fault of their own. The Employment Security Department (Department) administers this system.

Under the Employment Security Act (Act), eligible unemployed workers receive benefits based on their earnings in their base year. Most covered employers pay contributions (payroll taxes) to finance benefits. The Act is to be liberally construed to reduce involuntary unemployment to the minimum.

I. BENEFITS

A. Eligibility

Benefits are payable to eligible unemployed workers. An individual is eligible to receive benefits if he or she: (1) worked at least 680 hours in covered employment in his or her base year; (2) was separated from employment through no fault of his or her own or quit work for good cause; and (3) is able to work and is actively searching for suitable work.

Most employment is covered under the Act. Employment excluded from coverage includes work performed by certain corporate officers, employees of churches and certain nonprofit organizations, and certain nonresident aliens who are temporarily in the United States to work.

Claimants must search for work according to customary trade practices and through other methods when directed by the Commissioner of the Department (Commissioner). "Suitable work" is employment in an occupation in keeping with the individual's prior work experience, education, or training (unless such work is not available in the general area). In most circumstances, "suitable work" is full-time. The Department must monitor the job search efforts of persons who have received five or more weeks of benefits.

B. Disqualification

Individuals are disqualified from receiving benefits if they leave work voluntarily without good cause or are terminated for work-connected misconduct or a felony or gross misdemeanor.

Good cause, as specified in the Act, means leaving work: (1) to accept other work; (2) because of illness or disability, after taking precautions to preserve employment status with the employer; (3) to relocate for the spouse's employer-initiated mandatory job transfer; and (4) to protect the claimant or an immediate family member from domestic violence. In addition, the Commissioner may determine that other work-related factors are good cause for leaving work.

"Misconduct" is an act or failure to act in willful disregard of the employer's interest where the effect is to harm the employer's business. If an individual is discharged for misconduct, the individual is disqualified from benefits for seven weeks and until he or she earns seven times his or her weekly benefit amount. If an individual is discharged for a felony or gross misdemeanor, the individual loses his or her wage credits from that employment.

C. Duration and Amount

The maximum amount payable in an individual's benefit year is the lesser of 30 times the individual's weekly benefit amount or 1/3 of the total gross wages in the base year. (This amount is commonly expressed in terms of duration. In those terms, the maximum duration of benefits is 30 weeks.)

The maximum weekly benefit amount may not exceed 70 percent of the average weekly wage, except that: (1) from July 1, 2002, through June 30, 2004, the maximum weekly benefit amount is frozen at \$496; and (2) from July 1, 2004, through June 30, 2010, the growth rate in the maximum weekly benefit amount is capped at 4 percent.

An individual's weekly benefit amount is 1/25 (4.0 percent) of the average of the individual's wages in the two quarters of the base year in which wages were highest.

II. FINANCING

The unemployment compensation system requires covered employers to pay contributions on a percentage of their taxable payroll, except for certain employers that are exempt and certain employers that reimburse the Department for benefits paid to these employers' former workers. The contributions of covered employers are held in trust to pay benefits to unemployed workers.

A. Tax Rates

For most covered employers, contribution rates are determined by the rate in the employer's assigned rate class under the tax schedule in effect for that calendar year. The employer's position in the tax array depends on the employer's layoff experience relative to other employers' experience. This relationship is determined by the calculation of a benefit ratio, which is the total benefits charged in the last four years to the employer's experience rating account divided by the employer's taxable payroll in the same period. Based on the relationship of employers' benefit ratios, employers are placed in one of 20 tax rate classes.

The rates in these classes are determined by the tax schedule in effect. The Act establishes seven different tax schedules, from the lowest schedule of AA through the highest schedule of F. The tax schedule in effect for any given calendar year depends on the fund balance ratio, which compares the unemployment insurance trust fund balance on June 30 of the previous year to the total payroll in covered employment in the state for the completed calendar year prior to that June 30. The tax schedule in effect for 2003 is schedule B.

Several types of covered employers are not qualified to be assigned a rate class. Nonqualified employers include those who do not report enough periods of employment during the previous two years. These new employers pay the average industry rate in their industry, as determined by the Commissioner, but not less than 1 percent. The average industry rate also applies to certain successor employers who were not employers at the time of acquiring a business. Until a new successor employer becomes a qualified employer, the rate for a successor employer is the lower of the rate assigned to its predecessor or the average industry rate with a 1 percent minimum rate. For delinquent employers, the contribution rate is 5.6 percent.

Both qualified and nonqualified employers also may be required to pay an insolvency surcharge of 0.15 percent. This surcharge is added to all contribution-paying employer rates for rate year 2004 (unless the fund balance ratio is above a specified level).

B. Taxable Wage Base

The amount of tax that an employer pays is determined by multiplying the employer's tax rate by the employer's taxable wage base. The taxable wage base is the amount of each employee's wages subject to tax for a given rate year. This amount increases by 15 percent each year from the previous year's taxable wage base, with a cap of 80 percent of the state "average annual wage for contribution purposes." The "average annual wage for contribution purposes" is based on the average of the three previous years' wages. "Wages" includes "the cash value of all compensation paid in any medium other than cash."

C. Experience Rating

Under the experience rating system, most benefits paid to claimants are charged to their base year employers' accounts. In the case of multiple base year employers, benefit charges are prorated in proportion to wages paid.

Some benefits, however, are pooled costs within the system and are generally referred to as socialized costs. One kind of socialized cost is "noncharged benefits." Benefits that are not charged to employer accounts include benefits paid to claimants who requalify after a "voluntary quit" and benefits paid to claimants found to be marginally attached to the labor force. Other socialized costs include "ineffective charges" that occur when the benefits charged to an employer's account exceed the contributions that the employer pays. Costs are also socialized when an employer has an "inactive account," such as after going out of business, and is unable to pay contributions that were assessed.

D. Penalties

Employers who fail to file timely and complete quarterly unemployment tax reports are subject to a minimum penalty of \$10 per violation plus a percent of the amount that is delinquent for the first, second, and third month of delinquency.

Summary of Amended Bill:

Numerous provisions of the Act governing benefits and contributions are modified. The direction that the Act be liberally construed is deleted.

I. BENEFITS

A. Eligibility

Work by nonresident immigrants in the H-2A (agricultural guest worker) and H-2B (other guest worker) programs is excluded from covered employment.

Work search requirements are modified in several ways. Claimants who fail to actively search for work in accordance with the Act lose benefits for weeks in which they were not in compliance and must repay those benefits.

The customary trade practices that claimants must follow when searching for work are modified. If a labor agreement or dispatch rules applies, such customary trade practices must be in accordance with the applicable agreement or rules.

The requirement that "suitable work" be full-time work is modified. For part-time workers, "suitable work" includes work for 17 or fewer hours per week. "Part-time workers" are defined as those workers who earn wages in at least 40 weeks of the base year and who do not earn wages in more than 17 hours per week in any weeks of the

base year.

The Department's job search monitoring duties are increased. In addition to its existing duties, the Department must contract with employment security agencies in other states to ensure that out-of-state claimants in those states are actively engaged in searching for work in accordance with Washington job search requirements. The Department also may use certain electronic means to ensure that individuals are subject to job search monitoring, regardless of whether they reside in Washington or elsewhere.

These changes generally apply beginning with claims that are effective on or after January 4, 2004.

B. Disqualification

The reasons specified in the Act as good cause for leaving work voluntarily are limited. Individuals are not disqualified from receiving benefits if they leave work voluntarily for the following reasons: (1) to accept other work; (2) illness or disability, so long as the individual is not entitled to reinstatement; (3) to relocate for the spouse's mandatory military transfer; (4) to protect the claimant or an immediate family member from domestic violence; (5) a reduction of 25 percent or more in compensation or hours; (6) a change in the worksite that causes increased distance or difficulty of travel; (7) deterioration of work site safety; (8) illegal activities in the worksite; or (9) a change in the individual's usual work that violates his or her religious convictions or sincere beliefs. The Commissioner's discretion to determine that other work-related factors are good cause for leaving work is eliminated.

The definition of "misconduct" is changed, and related requalification requirements are increased. "Misconduct" is redefined as willful or wanton disregard of the employer's or another employee's rights, deliberate violations or disregard of standards of behavior, carelessness or negligence that causes or would likely cause serious bodily harm to the employer or another employee, or carelessness or negligence that shows an intentional or substantial disregard of the employer's interest. An individual who is discharged for misconduct is disqualified from receiving benefits for 10 weeks and until he or she earns 10 times his or her weekly benefit amount.

A definition of "gross misconduct" is added, and related penalties are increased. "Gross misconduct" is defined as a criminal act in connection with an individual's work, or conduct that demonstrates a flagrant and wanton disregard for the employer's or another employee's rights. An individual who is discharged for gross misconduct has his or her wage credits based on that employment or 680 hours of wage credits, whichever is greater, cancelled.

These changes generally apply beginning with claims that are effective on or after

January 4, 2004.

C. Duration and Amount

The maximum benefits payable are reduced. Beginning in the first month after the Commissioner finds that the state's unemployment rate is 6.8 percent or less, the maximum benefits payable are the lesser of 26 times the weekly benefit amount or 1/3 of the total gross wages in the base year. (The maximum duration of benefits is 26 weeks.)

The maximum weekly benefit amount is also reduced. For claims with an effective date on or after January 4, 2004, the maximum weekly benefit amount is 63 percent of the state average weekly wage or \$496, whichever is greater.

The formula for calculating an individual's weekly benefit amount is modified. For claims with an effective date on or after January 4, 2004, an individual's weekly benefit amount is 3.9 percent (instead of 4.0 percent) of the average of the individual's wages in the two quarters of the base year in which wages were highest.

II. FINANCING

A. Tax Rates

A new tax array with 40 rate classes is created beginning in rate year 2005. Employers are assigned one of the 40 rate classes based on the employer's benefit ratio.

Qualified employer rates are the sum of two separate rates:

- The array calculation factor rate is determined by the rate class, and ranges from 0.0 percent in rate class 1 to 5.4 percent in rate class 40.
- The graduated social cost factor rate is determined by calculating the flat social cost factor rate and multiplying by a graduated social cost factor that ranges from 78 percent to 120 percent of the flat social cost factor depending on the rate class.

The sum of the array calculation factor rate and the graduated social cost factor rate may not exceed 6.0 percent for certain seasonal industries (fishing, agriculture, and food processing) and 6.5 percent for other industries, except when a solvency surcharge applies.

Nonqualified employer rates are also the sum of two separate factors.

- For a new employer, the array calculation factor is the average industry rate plus 15 percent of that rate, but not more than 5.4 percent (the rate in rate class 40). The graduated social cost rate is the average industry rate plus 15 percent of that rate, but

not more than the rate assigned to rate class 40.

- A successor employer with substantial continuity of ownership or management of the predecessor's business must pay at the rate assigned to the predecessors and will have the experience of the predecessors transferred to its account as part of the array calculation factor rate beginning in January following the transfer. A successor employer that has acquired two or more businesses must pay at the rate assigned to the predecessor employer with the largest taxable payroll, rather than the highest tax rate class, until it qualifies for its own rate.
- For delinquent employers, the array calculation factor rate is 5.6 percent (two-tenths higher than the rate in rate class 40) and the graduated social cost rate is the same rate as the rate assigned to rate class 40.

A solvency surcharge of up to 0.2 percent replaces the insolvency surcharge. This surcharge is added to all contribution-paying employer rates for a particular rate year only if the fund balance is determined to be an amount that will provide fewer than six months of unemployment benefits.

B. Taxable Wage Base

Beginning in 2007, the state "average annual wage for contribution purposes" is determined using wage data from the previous year (rather than by averaging wage data from the three years prior to the calculation). Income attributable to the exercise of stock options is excluded from "wages" for contribution purposes.

C. Experience Rating

The charging of benefits paid to claimants who separated from employment for certain work-related reasons is changed beginning with benefits charged for claims that have an effective date on or after January 4, 2004. These benefits are charged to the experience rating account of only the separating employer. The work-related reasons are: (1) leave to accept other work; (2) reduction of 25 percent or more in compensation or hours; (3) change in work site that causes increased distance or difficulty of travel; (4) deterioration of work site safety; (4) illegal activities in the worksite; and (5) change in usual work that violates the individual's religious convictions or sincere beliefs.

The noncharging of benefits paid to claimants who are marginally attached to the labor force is eliminated.

D. Penalties

Penalties for certain employer delinquencies and/or misrepresentations are established. If quarterly tax reports are not timely or complete, the penalty is \$250 or 10 percent of the

contributions, whichever is less. If there is a knowing misrepresentation of payroll, the penalty is 10 times the amount of the difference in contributions that were paid and that should have been paid, and audit costs. If the delinquency is due to an intent to evade the successorship provisions, the penalty is the assignment of the maximum tax rate for five quarters.

III. ADMINISTRATION

The Department must require claimants filing claims telephonically or electronically to provide additional proof of identity.

The Department must conduct several studies and report its findings and recommendations to the Legislature by December 1, 2003. In consultation with a business-labor advisory committee, the Department must identify programs funded with special administrative contributions. The Department also must review employer turnover in the unemployment compensation system. Finally, the Department must study the potential for year to year volatility in the rate classes to which employers are assigned.

The Act is modified to specify that various funds in the unemployment insurance system must be used solely for unemployment insurance purposes.

Appropriation: Senate Bill 6099 appropriates \$11.5 million from Reed Act funds to implement Second Engrossed Substitute Bill 6097.

Fiscal Note: Not requested.

Effective Date of Amended Bill: The bill contains an emergency clause and takes effect immediately.

Testimony For: None.

Testimony Against: None.

Testified: None.