

# HOUSE BILL REPORT

## EHB 2255

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### As Passed Legislature

**Title:** An act relating to making adjustments to improve benefit equity in the unemployment insurance system.

**Brief Description:** Making adjustments to improve benefit equity in the unemployment insurance system.

**Sponsors:** By Representatives Conway, Simpson and Wood.

**Brief History:**

**Committee Activity:**

Commerce & Labor: 3/2/05 [DP].

**Floor Activity:**

Passed House: 4/1/05, 56-41.

Senate Amended.

Passed Senate: 4/15/05, 25-20.

House Concurred.

Passed House: 4/18/05, 57-38.

Passed Legislature.

### Brief Summary of Engrossed Bill

- Until July 1, 2007, calculates weekly unemployment benefits for new claims using 3.85 percent of the claimant's average wages during the two quarters of the base year in which the wages were highest, and does not charge these benefits to employers' experience rating accounts to the extent that the benefits exceed the amount that would have been paid if calculated as 1 percent of total wages.
- Restores the requirement for liberal construction of the unemployment insurance system until June 30, 2007.
- Through calendar year 2007, makes several adjustments in the social cost factor, including making the social cost factor rate zero for employers in certain industries, including agriculture, food processing, and fishing industries.
- Establishes the Joint Legislative Task Force in Unemployment Insurance Benefit Equity to review the unemployment insurance system, including whether the benefit structure is equitable, whether the structure fairly accounts for changes in workforce and industry work patterns, including seasonality, and claimant work

patterns, whether the tax structure equitably distributes taxes, and whether the trust fund is adequate in the long-term.

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## HOUSE COMMITTEE ON COMMERCE & LABOR

**Majority Report:** Do pass. Signed by 4 members: Representatives Conway, Chair; Wood, Vice Chair; Hudgins and McCoy.

**Minority Report:** Do not pass. Signed by 3 members: Representatives Condotta, Ranking Minority Member; Sump, Assistant Ranking Minority Member; and Crouse.

**Staff:** Chris Cordes (786-7103).

### **Background:**

The unemployment insurance system is a federal/state program under which employers pay contributions to fund unemployment compensation for unemployed workers. These payments are made under state unemployment laws and the Federal Unemployment Tax Act (FUTA). The FUTA allows the states' employers to receive a tax credit against their federal unemployment tax. The state receives a share of the federal FUTA revenues for administration of its unemployment insurance system, but only if the state maintains an unemployment insurance system in conformity with federal law. Washington's program is administered by the Employment Security Department.

In 2003, the Legislature enacted a number of changes to the unemployment insurance system. The changes included revisions to unemployment benefits and the tax system.

### Unemployment Benefits

Before January of 2004, a claimant's weekly benefit amount (WBA) was 4 percent of the claimant's average wages in the two quarters of the base year in which wages were highest. The 2003 legislation established new methods of calculating the WBA for claims with specified effective dates:

- *On or after January 4, 2004, and before January 2, 2005:* The WBA was calculated using 4 percent of the claimant's average wages in the three quarters of the base year in which wages were highest.
- *On or after January 2, 2005:* The WBA is 1 percent of the claimant's total wages in the base year.

The 2003 legislation also repealed a requirement for the unemployment insurance system to be "liberally construed."

### Unemployment Taxes

The 2003 legislation created a new unemployment tax system. Beginning with rate year 2005, the unemployment insurance contribution rate for most covered employers is

determined by the combined array calculation factor rate and the social cost factor rate, subject to a maximum rate, and solvency surcharge, if any. These rates are determined as follows:

- *Array calculation factor:* Employers are placed in one of 40 rate classes, with rates from 0 percent to 5.4 percent. The assigned rate class depends on the employer's layoff experience.
- *Social cost factor:* A flat social cost rate is calculated as the difference between benefits paid and taxes paid, divided by total taxable payroll. The amount is then adjusted for the months of benefits in the trust fund above 10 months, but the rate may not be less than 0.6 percent. Employers pay a graduated social cost factor rate, ranging from 78 percent to 120 percent of the flat rate, depending on the employer's rate class.
- *Maximum rate for the sum of the array calculation factor and the social cost factor:* For employers in fishing, agriculture, and food and seafood processing, the maximum rate is 6 percent. For employers in all other industries, the maximum rate is 6.5 percent.
- *Solvency surcharge:* Up to an additional 0.2 percent surcharge is added to the contribution rate in the next rate year if the unemployment trust fund has fewer than 6 months of benefits on a specified annual date.

Not all benefits paid are charged to the employers' experience rating accounts. By law, noncharging of benefits is required for specified reasons, and these costs are pooled within the system as social costs.

#### Federal Unemployment Funds

The FUTA tax paid by employers is held in the federal unemployment trust fund. These funds are deposited into two accounts that are used to pay the states' unemployment insurance systems' administrative costs and to pay extended unemployment benefits. By statute, these accounts may not exceed a specified monetary limit. If the limit is exceeded, the Congress may appropriate excess funds to the states under the Reed Act. In the federal Temporary Extended Unemployment Compensation Act of 2002, the Congress authorized a distribution of federal Reed Act funds to the states. Washington received approximately \$167 million. Of that amount, approximately \$130 million remains unappropriated. Reed Act funds may be used only for the limited purposes specified in federal law. These purposes include the payment of unemployment benefits and the administration of the unemployment system.

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#### **Summary of Engrossed Bill:**

The Legislature finds that the unemployment insurance system is falling short of its goals, and that the Legislature intends to adjust the balance between the goal of reducing the impacts of involuntary unemployment on workers and the desirability of reducing costs by making adjustments that allow reasonable improvements in benefit equity.

### Benefit Adjustments

The requirement that the unemployment insurance system be "liberally construed" when interpreting the system is restored until June 30, 2007.

For claims with effective dates on or after the first Sunday after the Governor signs the bill, and before July 1, 2007, the claimant's weekly benefit amount (WBA) is calculated using 3.85 percent of the claimant's average wages in the two quarters in the base year in which wages were highest. The benefits paid that exceed the benefits that would have been paid if the WBA had been calculated as 1 percent of annual wages are not charged to contribution paying employers' experience rating accounts.

### Social Cost Adjustments

For fiscal years 2006 and 2007, the social cost factor rate is zero for employers in agricultural crops, livestock, agricultural services, food and seafood processing, fishing, and cold storage.

For tax rate year 2007, the flat social cost factor is the lesser of the rate applicable with the new WBA calculations in effect or the rate that would have been applicable if the WBA had been calculated as 1 percent of a claimant's annual wages.

The formula is adjusted for determining the social cost factor in rate year 2007 to account for benefits that are not effectively charged because of these changes in the social cost factor.

When paying unemployment benefits, beginning in fiscal year 2006 and through calendar year 2007, funds are first requisitioned from the Reed Act funds in the amount of the benefits that are not effectively charged because the social cost factor rate is reduced to zero for certain industries and in the amount of benefits paid that exceed the benefits that would have been paid if the WBA had been calculated as 1 percent of a claimant's annual wages.

### Studies and Reports

The Joint Legislative Task Force on Unemployment Insurance Benefit Equity is established with four business representatives, four labor representatives, and the chairs and ranking minority members of the Senate Labor, Commerce & Research & Development Committee, and the House Commerce & Labor Committee. The Task Force must review the unemployment insurance system, including whether the benefit structure is equitable, whether the structure fairly accounts for changes in workforce and industry work patterns, including seasonality, and claimant work patterns, whether the tax structure equitably distributes taxes, and whether the trust fund is adequate in the long term. The Task Force must report to the Legislature by January 1, 2006.

The Employment Security Department is required to report to the Legislature annually for two years, beginning October 1, 2006, on the impact of the bill's provisions on the unemployment trust fund. The Employment Security Department is authorized to add two additional full-time equivalent employees to establish additional capacity in the Department to develop economic models for estimating the impacts of policy changes on the unemployment insurance system and the unemployment trust fund.

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**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill contains an emergency clause and takes effect immediately.

**Testimony For:** (Original bill) Construction workers were particularly hurt by the 2003 unemployment insurance bill. Construction goes on year-round and should be understood as an industry that is impacted by economic cycles and weather, but is not seasonal. Many workers depend solely or heavily on unemployment benefits during the periods between jobs. Construction workers cannot always move immediately to the next construction job. Workers could plan for and manage to live on benefits at the previous levels, but the change to three-quarter averaging, and now to four-quarter averaging, is crippling to many. At least 33 states use some form of two-quarter averaging, which should be the standard. Surveys of workers show how many live on the edge and how fragile their economic security is. The lost benefits translate into large losses in purchasing power in the community. Last year, about \$52 million was lost in purchasing power under three-quarter averaging and the loss could double under four-quarter averaging. There was no public hearing to warn of the drastic benefit cuts that resulted from the 2003 legislation. It is not clear that the Legislature or the public realized the impact that the bill would have on workers and communities. Those workers who are hardest hit are those who do not determine when work is available. Even those at the maximum benefit amount will see a large cut. There is a need to correct the benefit inequity in the system. The 2003 bill resulted from failed negotiations and might have been harder to pass if there had been public input.

(Original bill, with concerns) The business community is generally opposed to the concept of opening up the unemployment insurance system at this time. The state still has the highest unemployment taxes, and the system needs the balance that was inacted in 2003. Those changes had very broad support and participation in crafting, while the previous 2002 legislation had a much narrower base of support. The 2003 bill did not reduce costs for all industries and, for example, the construction industry is paying more as part of the deal. Any changes that do not recognize the balances and relationships within the system could throw the trust fund into insolvency and be detrimental to the state's economy. However, the concerns about benefit equity are recognized. Any solution must keep in mind certain principles, including the need to address seasonal issues, to avoid cost shifting, to maintain solvency of the system, and to keep costs at no more than 200 percent of the national average. In considering this legislation, it would be useful to establish the principles that would guide what everyone is trying to achieve. There should be a recognition that the previous legislation addressed an inequity in how the unemployment system was paid for and that the seasonal industries need relief from an unfair burden. While there was broad support for the 2003 bill, some industries' concerns were not fully addressed. For example, there was general agreement that if the system was reopened to amendment, the seasonal industries should have their concerns addressed. Both agricultural workers and employers took a hit under the 2003 legislation. Many employers in the industry immediately rose to the top rate of 6 percent.

When that industry's workers file claims every year, the employer cannot pay enough in taxes to cover the cost. There should be full public discussion and an understanding of all perspectives as part of working on this issue.

**Testimony Against:** None.

**Persons Testifying:** Dave Johnson, Washington State Building and Construction Trades Council; Pam Crone, Unemployment Law Project; and Jeff Johnson, Washington State Labor Council.

(With concerns) Mellani McAleenan, Association of Washington Business; Jan Gee, Washington Retail Association and Washington Food Industry; Rick Slunaker, Association of General Contractors; and Chris Cheney, Washington Growers League.

**Persons Signed In To Testify But Not Testifying:** None.