

**Testimony of Eric J. Oxfeld, President
UWC – Strategic Services on Unemployment & Workers’
Compensation
before the
Subcommittee on Children and Families
of the
Senate Committee on Health, Education, Labor & Pension
The Honorable Judd Gregg, Chairman
July 14, 1999**

Mr. Chairman, members of the Committee, my name is Eric Oxfeld. I am President of UWC – Strategic Services on Unemployment & Workers’ Compensation, which is the only national business advocacy association exclusively devoted to unemployment insurance (UI) and workers’ compensation issues. Our members are employers of all sizes and industries, as well as business associations and service organizations, who share our interest in maintaining a sound UI program for workers and employers. UWC also manages the National Foundation for Unemployment Compensation & Workers’ Compensation, which conducts research and educational activities related to these programs and publishes the annual HIGHLIGHTS OF STATE UNEMPLOYMENT COMPENSATION LAWS book. Thank you for the invitation to appear before you today to address the Clinton Administration’s proposal to divert state UI benefit trust funds to provide paid leave under the Family and Medical Leave Act (FMLA).

UWC strongly supports the federal-state UI program, which has served workers and employers for nearly 70 years. Financed by federal and state payroll taxes paid by employers, UI has been a success in providing temporary support and re-employment services for workers who lose their jobs when their employers no longer have work available. UI not only encourages stability in employment, it provides a critically important counter-cyclical balance for the nation’s economy during economic downturns. It is axiomatic that UI trust funds must be built up during periods of prosperity so that in recessionary times money will be available to pay jobless workers without increasing payroll taxes when business can least afford it.

On May 23, President Clinton directed the U.S. Department of Labor (DOL) to reverse longstanding Federal Unemployment Tax Act (FUTA) standards and thereby permit workers who are on leave under the Family and Medical Leave Act to simultaneously collect UI benefits. He has also directed the Department to develop model state legislation to promote this objective.

UWC is strongly opposed to the diversion of UI trust funds to provide paid leave under FMLA. **UI and FMLA serve different and incompatible purposes.** UI is a reemployment program, and UI funds are dedicated by law to protect workers who lose their jobs when the *employer* no longer has work available. UI benefits are payable only while the worker seeks new work and cease upon an offer of suitable work. FMLA leave is for workers who *have a job* but took time off for personal medical reasons. By definition, **workers on FMLA leave are not unemployed**, because they have jobs.

The Administration UI/FMLA initiative **opens the door to further UI diversions** and will establish a duplicative, rigid, costly, **single-payor government program** paying compensation for disability, sick leave, and FMLA leave, which many employers now provide voluntarily as a more flexible and less costly employee benefit.

UWC is especially troubled by the process – or, more accurately, lack of process – followed by the Administration on the UI/FMLA issue. The proposal equates to legislating through the Executive Branch. A presidential directive, with no opportunity of any kind for public input, simply ordered the Secretary of Labor to promulgate regulations permitting a UI diversion to pay for FMLA leave. Only *after* these regulations are issued, the Secretary is directed to study the impact of such a

change. Given the history of the UI program and the debate over paid leave under FMLA, the public has the right to expect that a fundamental change to the UI and FMLA programs will be thoroughly -- and publicly -- reviewed by Congress and the public *before* any decision is made about its wisdom -- or legality.

Federal UI law, as embodied in the Federal Unemployment Tax Act (FUTA), contains a limited number of requirements with which state UI laws must conform. The penalty when a state UI law is out of conformity with the FUTA requirements is an **increase in the FUTA tax rate on employers from .8% to 6.2% -- a more than 700% increase.**

The UI/FMLA proposal puts employers at risk of this 700% tax increase, because allowing **UI payments to workers is directly contrary to nearly 70 years of federal UI jurisprudence.** Until now, DOL has always enforced the FUTA as requiring state laws to limit UI benefits to claimants who are available for work. DOL's Bureau of Employment Security (now the Unemployment Insurance Service) articulated this position when it stated that "The qualifying requirement and the requirement that claimants be able and available for work are the two halves of a single requirement that protection be limited to unemployed members of the labor force." This view was embodied in a 1997 letter to Vermont, in which DOL took the position that a proposal to pay for family leave out of UI taxes would violate conformity requirements.

Grafting onto the unemployment insurance system the wholly alien responsibility to finance and deliver paid family and medical leave to workers who by definition have jobs and are not available for employment will financially and administratively burden the UI system and those whom it sustains. In short, using UI trust funds for paid FMLA leave means that jobless workers and employers will no longer be able to count on the protections afforded by UI.

While UI is clearly a success, it suffers from a number of serious problems that must be addressed if it is to continue serving its traditional role -- much less, take on new responsibilities. For example, taxes collected from employers under FUTA are 25% higher than needed for efficient administration of UI benefits and operation of the labor exchange under the Wagner-Peyser Act -- the purposes for which FUTA funds are dedicated by law. The reason for this imbalance is a "temporary" FUTA surtax enacted in 1976 to provide funds to reimburse depleted trust fund accounts that have long since been restored. The Taxpayer Relief Act of 1997 extended this surcharge through the year 2007. There is no justification for the 30 year extension of this "temporary" tax surcharge.

Not only are employers being overtaxed under FUTA, but appropriations from this dedicated source of administrative funds have been cut. In 1997, 49 of the 53 states and jurisdictions receiving administrative funding for UI and state employment service functions received less than the FUTA taxes collected from employers in those states. Since 1990, less than 58 cents of every employer FUTA tax dollar has been returned in administrative funding for states. From 1993 to 1997, FUTA tax collections increased from \$4.23 billion to \$6.45 billion while administrative funding was cut from \$3.81 billion to \$3.36 billion. The return of employer taxes to the states has been an increasingly smaller percentage with each year and is now down to under 52%.

During the tight labor market we are now experiencing, it is astonishing that the United States is still spending \$30 billion a year on UI. Despite widespread labor *shortages* in many parts of the country, **the average duration of UI claims has climbed** to more than 14 weeks at least one week longer than expected for today's low unemployment. The severe under-funding of UI administration and state employment services is a direct cause of this extended claim duration, because state UI agencies lack the resources needed to weed out improper claims and provide re-employment services. Longer claim duration means that state UI taxes are higher -- and state trust fund balances are lower -- than they should be. Moreover, inadequate FUTA funding has forced 42 states to dip into state treasuries for more than \$200 million in additional taxes (mostly paid by employers).

Of equal concern is the solvency of state UI trust funds. While UI trust fund reserve levels may not be drawing much public attention at the moment, given the lowest unemployment rates in 30 years, there have been a number of occasions when the federal government has been forced to “bail out” states which depleted their UI funds. During the 1980-82 recession, for example, 32 states were forced to borrow from the federal government to meet their UI benefit obligations. At the peak of borrowing in 1983, the federal government extended loans to the states totaling more than \$13 billion.

The U.S. Department of Labor (DOL) has been outspoken of late in expressing concern that **state UI reserves are inadequate**. DOL recommends that states use a solvency test called the “average high cost multiple” (AHCM). To satisfy the AHCM, a state must keep sufficient reserves in its UI trust account to cover benefit costs for its 3 highest-cost years during the past 20 years or past 3 business cycles, whichever is longer. The attachment contains a table published by DOL which displays each state’s trust fund balance and AHCM rating for 1998. A rating of less than 1.0 indicates inadequate reserves under DOL’s standard. As the attachment shows, 20 states fail the AHCM test, as does the country taken as a whole, and most other states are only marginally above it. At current reserve levels, DOL estimates that 25 - 30 states would need to borrow \$20 - 25 billion in order to pay benefits if an economic downturn like the 1980-82 recession occurs.

As a result of DOL’s concern over adequate reserve adequacy, in both the 105th and 106th Congresses the Administration has asked Congress to enact legislation (“UI Safety Net” proposal) that, among other provisions, would give states additional financial incentive to build up their trust funds.

Ironically, one of the biggest deterrents to maintaining higher state reserves is the risk of diversions once the funds have been built up. Employers have learned the hard way that there is a powerful temptation to divert these funds by expanding the system – e.g., by using UI as paid leave under FMLA. The threat of these diversions is the precise reason that Congress, when it established the UI system, mandated that state UI taxes could be expended only on unemployment benefits. This stricture is very tight. Even UI *administrative* costs cannot be financed out of state UI taxes.

Workers as well as employers have a direct stake in the solvency of the UI program. The large debts states incurred in the 1980’s forced them to curtail benefit eligibility and make other changes designed to reduce UI benefit costs to get back in the black and remain solvent. A diversion to pay for FMLA leave will further deplete funds available for jobless workers.

It is time for a change in UI, but not in the direction of the UI/FMLA proposal! We need a UI system that properly funds states for administration and minimizes the tax burden on the employers who pay for it.

A coalition of 28 states and over 90 state and national employer organizations representing millions of employers have formed a coalition for reform of employment security financing. Senator Mike DeWine has introduced a bill, S. 462, designed to reform the UI system, as recommended by the Coalition.

S. 462 has been carefully crafted to address the federal/state partnership, appropriate funding levels, and employer taxes. This proposal includes provisions to:

- Repeal the .2% FUTA surtax;
- Transfer responsibility for collection of the FUTA tax to the states;
- Provide adequate dedicated funds for administration of the UI program and public employment services; and

- Increase the flexibility of the use of UI funds as part of the workforce development system designed by each state.

As it has recently done to protect Social Security, we urge Congress to ensure that unemployment insurance trust funds continue to be available to protect workers and employers. ***We respectfully urge you to actively support proposals to (1) preclude the Administration from advancing its UI/FMLA proposal, which is a fundamental change in the unemployment system that jeopardizes the future of the nation's UI system and the unemployed individuals whom the Trust Fund was established to protect, and (2) support S. 462, UI reform legislation which will provide improved services to workers and employers, reduce FUTA payroll taxes on business, and help move UI claimants off unemployment rolls and into jobs.***