

## Preserve UI Reform To Preserve Jobs

### THE BOTTOM LINE

The 2003 unemployment insurance reform legislation improved the balance in a system that had imposed the nation's highest employer UI taxes, combining extraordinary benefits with lax enforcement standards.

Now, fewer than two years later and before the reforms have taken full effect, reform opponents want to revisit the legislation, contending it went too far.

It did not.

Now is not the time to retreat from the commitment made in 2003 to a stronger economy and a secure UI program.

In 2003, the Washington State Legislature reformed the state's Unemployment Insurance (UI) program. Although the term "reform" is often attached to legislative changes that amount to little more than modest statutory refinements, the 2003 UI legislation, SB 6097 fundamentally changed policy. The bill realigned benefits and costs to maintain the safety net for workers who have lost their jobs through no fault of their own and allocate equitably the tax burden among employers.

The legislation improved the balance in a system that had imposed the nation's highest employer UI taxes, combining extraordinary benefits with lax enforcement standards. For decades, our state's employers sought relief without success. And despite the overwhelming evidence that the system placed the state at a competitive disadvantage in the quest to create and sustain jobs and recruit and retain businesses, it's doubtful that lawmakers would have acted had the reform not been coupled with the incentive package designed to win the Boeing 7E7 (now called the 787).

In 2002, Boeing Commercial Airplane Company President Alan Mulally told the House Labor and Commerce Committee that of the 27 locations where Boeing operates, Washington has the highest unemployment insurance costs. Mulally's testimony, coupled with the intense interstate competition for the next generation plane, underscored the urgency of legislative action.

Business leaders hailed the legislation as "a major win" that would make the system "more efficient, cost effective" and better able to serve unemployed workers (Association of Washington Business 2003); organized labor said the reform "guttled" the UI system (Washington State Labor Council 2003, page 3).

Now, fewer than two years later and before the reforms have taken full effect, reform opponents want to revisit the legislation, contending that SB 6097 went too far. It did not. Despite the significant changes embraced by the legislation, Washington still has one of the nation's most generous, and therefore expensive, UI systems. Essential protections remain safe. The reforms sanded down many of the rough edges, but left the basic structure intact.

### WASHINGTON'S COSTLY UI SYSTEM

According to an analyst with the National Conference of State Legislatures (NCSL), in 2002 Washington State had the "most generous (UI) system in the country." (Association of Washington Business 2002,

page 1) The 2003 UI reform will over time bring us more in line with other states.

The full impact of the reforms has not been immediate because the reforms are being phased in, as we describe below. The reduction in the maximum weekly benefit will not be fully effective until 2007 or 2008. Changes in

the way that weekly benefits are calculated decreased total payout by 7.1 percent in 2004. For 2005, the margin should grow to 16 percent.

Nonetheless, when compared with the nation, the reformed UI program does not seriously diminish Washington's reputation for generosity.

Washington employers pay an average tax of \$755 per employee, the highest in the nation and more than two and a half times the U.S. average. (See Table 1 comparing 2001 with 2004). As the table shows, the average per-employee tax figures indicate some volatility over time. Prior to the recession, many states had significantly reduced UI taxes, enjoying the benefits of healthy reserves, decent investment returns, and low payouts. In the subsequent years, taxes have risen. The U.S. average climbed to \$272 from \$178. But at the top of the rankings, the rankings have not changed much. Alaska led in 2001; it ranks second to Washington now. Oregon moved from fourth to third; Massachusetts from sixth to fourth.

Key factors in the high tax burden are costs of the maximum weekly benefit amount and the length of time unemployed workers can receive benefits. Washington ranks near the top on both measures, receding only slightly as a result of the reform.

Reflecting the high maximum, Washington ranked fifth in the nation in the average weekly benefit amount (AWBA) paid in the third quarter of 2004, paying \$310 per week. That's twenty percent higher than the U.S. average, as shown in Table 2.

In 2004, Washington ranked seventh in the average length of time unemployed workers received benefits, about a week and a half longer than the U.S. average, as Table 3 indicates. Massachusetts ranked second.

## CRITICAL REFORMS

The 2003 reform affected most aspects of the state's UI system. In Table 4, several critical changes in benefits, eligibility, and taxation are summarized. Some policy changes were phased in over 2004; the table shows policies effective in January 2005.

Table 1: Unemployment Insurance Taxes

	2004 - 3rd Qtr		2001 - 3rd Qtr	
	Per Employee	Rank	Per Employee	Rank
Washington	\$755	1	\$557	2
Alaska	\$678	2	\$676	1
Oregon	\$648	3	\$450	4
Hawaii	\$465	4	\$352	6
Massachusetts	\$462	5	\$248	12
Connecticut	\$450	6	\$210	16
Rhode Island	\$434	7	\$360	5
New Jersey	\$413	8	\$470	3
New York	\$366	9	\$255	11
Illinois	\$363	10	\$189	21
Michigan	\$342	11	\$247	13
Pennsylvania	\$336	12	\$288	9
Idaho	\$331	13	\$331	7
Minnesota	\$330	14	\$189	22
North Dakota	\$296	15	\$209	17
Iowa	\$296	16	\$223	15
Nevada	\$286	17	\$272	10
North Carolina	\$275	18	\$109	33
California	\$273	19	\$182	23
Wisconsin	\$263	20	\$200	19
Arkansas	\$240	21	\$162	25
Montana	\$231	22	\$208	18
West Virginia	\$224	23	\$232	14
Texas	\$216	24	\$108	34
Oklahoma	\$215	25	\$42	50
District of Columbia	\$207	26	\$198	20
Kentucky	\$200	27	\$136	29
Tennessee	\$196	28	\$105	35
Maryland	\$187	29	\$119	31
Utah	\$182	30	\$110	32
Maine	\$180	31	\$324	8
Ohio	\$180	31	\$126	30
Delaware	\$170	33	\$145	27
Kansas	\$168	34	\$104	37
Missouri	\$160	35	\$98	38
Vermont	\$160	35	\$160	26
Wyoming	\$159	37	\$176	24
Indiana	\$154	38	\$77	43
New Mexico	\$151	39	\$143	28
Colorado	\$150	40	\$90	42
South Carolina	\$147	41	\$98	39
Georgia	\$145	42	\$43	49
Alabama	\$144	43	\$96	40
Mississippi	\$140	44	\$91	41
New Hampshire	\$128	45	\$64	46
Virginia	\$120	46	\$48	48
Florida	\$119	47	\$77	44
Louisiana	\$119	47	\$105	36
Nebraska	\$119	47	\$70	45
Arizona	\$70	50	\$63	47
South Dakota	\$49	51	\$42	51
United States	\$272		\$178	

Source: U. S. Department of Labor

## Construction

A subtle and important change is in the direction given the department and courts regarding construction of the statute. The reform eliminated the requirement that the statute “shall be liberally construed,” which effectively shifted the burden of proof to employers in any contested claim.

Today, workers and employers contend on an equal basis.

## Taxes

The overall level of UI taxation is set to achieve an adequate balance in the UI trust fund, from which benefits are paid. The tax burden is distributed among employers based in part on their specific claim experiences. Stable employers pay less than employers who lay off workers regularly and therefore draw more on the UI system. Not all costs are directly assigned to individual employers, however, and these “socialized costs,” are spread across the employer base. SB 6097 tackled the difficult challenge of matching tax liability with employer responsibility, an issue that sparked conflict within the business community – where there has long been disagreement regarding the way costs have been allocated – but little controversy outside the network of affected employers. The reform replaced the state’s matrix of 20 rate classes and seven schedules of contribution rates with a 40 rate class schedule. The new schedule tops out at 6.5 percent for most industries and better reflects employer experience, reducing cost-shifting.

## Marginal Labor Force Attachment

As reported in the 2002 WashACE case study, “*Generous Unemployment System Also Costly*,” Washington’s Marginal Labor Force Attachment (MLFA) provision – unique to our state – accounted for nearly 25 percent of the state’s non-charges (socialized costs assigned to the whole system, rather than an identified employer). Under this provision, employers were relieved of responsibility for charges involving employees with irregular earnings patterns. By eliminating MLFA, the reform reduced the socialized costs borne by all employers, increasing system equity and accountability.

## Benefits

The reform made three important changes in UI benefits: reducing the maximum length of time claimants can receive bene-

Table 2: Average Benefit and Duration, 2004 3rd-Quarter

	Average Weekly Benefit		Average Duration	
	Amount	Rank	Weeks	Rank
Massachusetts	\$345	1	19.3	2
Hawaii	\$319	2	15.8	26
New Jersey	\$317	3	18.6	5
Rhode Island	\$313	4	15.7	27
Washington	\$310	5	17.9	7
Minnesota	\$306	6	16.2	18
Colorado	\$296	7	15.1	31
Michigan	\$289	8	14.6	33
Pennsylvania	\$284	9	17.8	9
Connecticut	\$272	10	17.7	10
Illinois	\$269	11	19.2	3
New York	\$268	12	18.8	4
California	\$266	13	18.3	6
Kansas	\$265	14	16.4	17
Indiana	\$263	15	13.7	43
Utah	\$263	16	13.7	43
Kentucky	\$260	17	14.2	35
Texas	\$258	18	16.6	14
North Carolina	\$257	19	14.0	39
District of Columbia	\$255	20	20.5	1
Iowa	\$254	21	13.9	41
Maryland	\$253	22	16.0	21
Oregon	\$252	23	16.5	15
Delaware	\$249	24	15.9	23
New Hampshire	\$248	25	17.2	11
Vermont	\$248	26	14.4	34
Ohio	\$243	27	16.1	20
Nevada	\$243	28	15.4	28
Virginia	\$241	29	13.4	46
Wisconsin	\$239	30	14.0	39
Wyoming	\$239	31	12.5	50
Georgia	\$239	32	12.5	50
Maine	\$235	33	16.5	15
New Mexico	\$228	34	17.9	7
Arkansas	\$226	35	14.2	35
Idaho	\$222	36	13.5	45
Florida	\$221	37	15.9	23
West Virginia	\$221	38	15.4	28
Nebraska	\$216	39	13.9	41
Oklahoma	\$215	40	16.8	13
North Dakota	\$211	41	12.6	49
South Carolina	\$210	42	14.2	35
Tennessee	\$209	43	14.1	38
Missouri	\$202	44	15.9	23
South Dakota	\$202	45	12.8	47
Alaska	\$195	46	15.0	32
Louisiana	\$194	47	16.0	21
Montana	\$184	48	16.2	18
Alabama	\$176	49	12.7	48
Arizona	\$176	50	16.9	12
Mississippi	\$171	51	15.3	30
United States	\$258		12.5	

Source: U. S. Department of Labor

**Table3: Summary of the 2003 Unemployment Insurance Reforms**

	<u>Before Reform</u>	<u>After Reform</u>	<u>Effect</u>
<b>Construction:</b>	Calls for liberal construction of the program.	Provision requiring liberal construction is repealed.	Eliminates presumption favoring worker.
<b>Tax Rates:</b>	Set out in a table with 20 rate classes and levels ranging from AA to F	The tax table consists of 40 fixed array classes from 0.00 percent to 5.4 percent.	Taxes more accurately reflect employer experience; more equitable distribution of "socialized costs."
<b>Benefit Calculation:</b>	1/50 of total earnings in the two highest earning quarters (2 quarter averaging)	1/100 of the total earnings in the prior year (4 quarter averaging)	Benefits will more directly reflect claimants work experience; \$164 million annual savings estimated.
<b>Maximum Weekly Benefit Amount:</b>	70 percent of average weekly wage of workers in the state; set at \$496 in 2003.	Changed to the greater of \$496 or 63 percent of average weekly wage paid in prior year. Expected to stay at \$496 for at least five years.	Expected to save more than \$17 million per year for the time the benefit is frozen.
<b>Duration of Benefit:</b>	30 weeks	26 weeks (unless unemployment rate exceeds 6.8 percent)	Puts Washington in line with other states; 30 weeks was longest duration in nation. Estimated to produce \$57 million annual savings.
<b>Voluntary Quits:</b>	Provides general guidance regarding the granting of benefits to workers who voluntarily leave employment.	Identifies ten specific reasons for granting benefits to a worker who voluntarily quits.	Removed ambiguity by placing criteria in statute.
<b>Part-time Workers:</b>	Not covered	Allows workers earning wages in no more than 17 hours per week to receive benefits.	New benefit, expected to cost less than \$10 million annually.
<b>Marginal Labor Force Attachment:</b>	Employers relieved of responsibility for certain charges involving employees with irregular working patterns	MLFA repealed.	Shrinks "non-charges" (i.e., charges not attributed to an employer), assigns costs appropriately, and reduces amount of socialized costs borne by all employers.
<b>Misconduct:</b>	Requires proof of "harm to the employer's business."	No longer requires proof of harm to employer, new definition of gross misconduct, specifies acts that constitute misconduct.	Reduces standard of proof, provides clarity.
<b>Job Search:</b>	Requires claimants to demonstrate contacts with at least three employers per week or in-person search activity at reemployment center.	Expands monitoring to include claimants collecting benefits outside Washington; requires three documented in-person search activities per week at reemployment center; failure to comply results in loss of all benefits for weeks during which claimant was not in compliance and repayment of benefits.	Strengthens job search requirements.

fits, and slowing the growth in both the maximum weekly benefit and the base upon which benefits are calculated.

Before the reform, unemployed workers could receive benefits for a maximum of thirty weeks. Only Massachusetts matched Washington in the allowed duration. All other states topped out at 26 weeks. SB 6097 capped the time limit at 26 weeks.

In 2003, the maximum weekly benefit amount was \$496, or 48 percent higher than the US average of \$336. In addition to shifting to a four-quarter average, the reform began an incremental reduction in the maximum weekly benefit amount. Previously, the maximum was set at 70 percent of the state's average weekly wage. The reform reduced the maximum to 63 percent, freezing the maximum at \$496 (after allowing a short bump to \$510) until \$496 equals 63 percent of the average weekly wage.

Seasonal workers will be most affected by another provision of the reform. Weekly benefits previously were calculated as 1/25th of the average quarterly wages of the claimants two highest quarters' wages during the base year. This "two quarter averaging" boosted benefits well above what they would have been had a full year's work history been considered. The reform moved to three quarter averaging in 2004 and began four quarter averaging this year. Effective January 2, 2005, the weekly benefit amount will be calculated as one percent of total wages received during the worker's base year.

Additionally, the legislation excluded stock options from the definition of wages for UI purposes.

### **Eligibility**

The reform tightened up two areas regarding employee eligibility for benefits: "voluntary quits" and employee misconduct. It also loosened one area: Part-time workers became eligible.

Unemployment insurance aims to provide wage replacement to workers who lose their jobs through no fault of their own—for example, workers who are laid off when a company cuts production or goes out of business. Still, the law recognizes some circumstances under which a person who voluntarily leaves his job should be eligible for unemployment benefits. Before SB 6097, the criteria for such determination had expanded and lacked statutory precision. The reform reduced the department's administrative discretion and clarified reasons for "good cause" voluntary quits. The legislation eliminates some causes (e.g., spousal relocations other than military transfers), adds some (e.g., leaving employment that violates religious convictions; leaving because of illegal activity at the work place); and preserves many existing good cause reasons (e.g., leaving to accept other work, illness or disability in the immediate family, domestic violence, major change in worksite).

Employees fired for misconduct do not qualify immediately for unemployment compensation. Prior to reform, however, employers had to demonstrate that the misconduct constituted "harm to the employer's business." That standard, which required a high level of proof, was eliminated in the reform bill. The bill specified behaviors that amount to misconduct, including willful disregard of an employer's or fellow employee's rights, deliberate violations of standards of behavior, dangerous carelessness or negligence.

Employees terminated because of misconduct cannot receive UI benefits for ten weeks, and then only regain eligibility if they earn wages equal to

ten times their weekly benefit amount in a subsequent job. Gross misconduct – newly defined as involving a criminal act or conduct that demonstrates flagrant disregard of the employer or a fellow employee – carries with it the loss of wage credits.

Part-time workers became eligible for benefits as a result of the reform. To qualify, the worker must be looking for part-time employment and have had wages in at least 40 weeks of the base period. Further, in that time, they must not have worked more than 17 hours a week.

### **Job Search**

UI is intended to be a bridge between jobs, so benefits are tied to requirements to look for work. Washington's search requirements have been lighter than those of many other states. SB 6097 strengthened the job search requirements and increased penalties for noncompliance.

### **CONCLUSION**

Improving the state's business climate requires constant attention to business costs, benchmarking against competitor states, and balancing costs with benefits. The 2003 UI reform mainstreams Washington's UI system. System costs had risen to such heights that they discouraged employers from adding jobs here, even threatening our ability to retain one of the state's industrial icons, The Boeing Company. And while the reform must be credited with helping Boeing decide to assemble its next generation of commercial airliners in Washington, the benefits of UI reform extend to virtually every employer here today as well as those arriving tomorrow.

Unemployment insurance provides transitional income for unemployed workers seeking jobs. By creating an environment that nurtures job creation, SB 6097 best serves those workers. Now is not the time for the legislature to retreat from the it made commitment in 2003 to a stronger economy and a secure UI program.

### **REFERENCES**

- Association of Washington Business. 2002. *"Generous" Unemployment System Also Costly*. WashACE Case Study.
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