HOUSE COMMITTEE ON APPROPRIATIONS

FISCAL NOTE

SENATE BILL NO. 1310 **PRINTERS NO.** 2234 **PRIME SPONSOR**: **Gordner**

COST / (SAVINGS)

FUND	FY 2011/12	FY 2012/13
Unemployment Compensation Trust Fund	**$0**	**($187,500,000)**
Debt Service Fund*	**$0**	**$390,043,000**
Reemployment Fund	**$0**	**$5,000,000**

(*Assumes $3.37 billion issue with 10-year maturity at 2.75% rate with level debt service. For total savings to employers please see Fiscal Impact on page 5)

SUMMARY: Amends the Unemployment Compensation Law to address the solvency of the Unemployment Compensation Trust Fund and refinance the outstanding debt owed to the federal government. This legislation would take effect immediately.

ANALYSIS: Amends the Unemployment Compensation Law to: 1) change partial benefit credit from 40% to 30% of weekly benefit rate; 2) stipulate that earnings for requalification for benefits must be in "employment"; 3) increase taxable wage base and decrease State Adjustment Factor; 4) change Interest Factor to bond debt repayment mechanism; 5) increase trigger solvency percentage to 250% from 125%; 6) enact various administrative changes, including allowing the collection of back payments through Treasury Offset Program; 7) change financial eligibility requirements in base year earnings (20% to 49.5% must be earned outside high quarter); 8) change effective date with respect to variable credit weeks (from January 1, 2015 to January 1, 2013); 9) permit the issuance of bonds for repayment of outstanding federal loans; 10) changes maximum benefit cap to maintain annual maximum benefit at $573 through 2019; and 11) create an amnesty program for collection of unpaid contributions or compensation overpayment.

<u>Partial Benefit Credit Adjustment:</u> Amends Section 4 (m)(3) to change definition of "Partial Benefit Credit" from 40% of weekly benefit rate to 30% of weekly benefit rate.

<u>Change to Requalification Requirements for Eligibility:</u> The definition for "Valid Application for Benefits" is changed in Section 4(w) to stipulate an individual's wages must be earned in “employment” (as defined under the law) for the purposes of a valid application for benefits. With respect to claimants who have been found ineligible for benefits due to a disqualifying separation from work, Section 401(f) is amended to clarify that wages earned during the minimum six-week requalification period must be earned in "employment", as defined under the law.

<u>Employer Tax Changes:</u> The legislation increases the taxable wage base from $8,000 to $10,000 over a period of six years (beginning in 2013 and ending in 2018), and it decreases the State Adjustment Factor (SAF) from 1.5% to 0.75% over the same six years.

Change in Interest Factor Assessment: The legislation amends Section 301.6 to direct revenues collected through the "interest factor" to: 1) pay solvency bond obligations and bond administrative expenses due for a particular calendar year; 2) replenish amounts which have been drawn from solvency bond reserves; 3) maintain adequate debt service coverage ratio; 4) fund early, optional, mandatory redemptions and purchases of outstanding solvency bonds which occur in a particular calendar year; 5) pay the interest on interest-bearing federal loans; and 6) repay outstanding loan advances.

The legislation will require contributions paid by employers under the law to first be directed toward meeting the employer's liability under the "interest factor" requirement. If excess monies are collected in a calendar year through the "interest factor", excess revenues may be applied toward the next year's obligations. The Interest Factor would be capped at 1.1%, and this cap would decrease to 1.0% for years after bond debt is paid in full.

U/C Trust Fund Solvency Trigger Change: The legislation adjusts the solvency trigger schedule to create a larger monetary reserve in Trust Fund. For calendar years 2013 through the year when federal loan balance/bond is paid off, if the trigger percentage on July 1 of preceding calendar year is less than 250%, the Secretary is tasked with determining the tax rates to raise: 1) $100 million through employer surcharge mechanism; 2) $225 million through additional employer contribution mechanism; 3) $166.67 million through the employee wage tax; and 4) $52 million through benefit reductions. For years in which federal debt/bond debt is paid off, and trigger percentage is less than 250%, the Secretary is tasked with determining the tax rates to raise; 1) $138 million through employer surcharge mechanism; 2) $310 million through additional employer contribution mechanism, plus 20% of amount that was transferred from Trust Fund to make bond service payments during previous 5 years, and 20% of amount not recoverable by additional contributions during previous 5 years; 3) $230 million through employee tax; and 4) $72 million through benefit reductions.

Administrative Changes: Section 304 of the law is amended to allow the department to mail assessments via email, and is amended to stipulate that the Office of General Counsel shall have supervision of rules of evidence/procedure under unemployment compensation appeals process. Section 308.1 is amended to eliminate need for the department to re-file liens every five years to maintain their validity. Section 309 is amended to add language formally recognizing the department's ability to collect contributions, interest, penalties and other liabilities under the U.S Treasury's "Treasury Offset Program" (TOP). Section 313 is amended to increase penalties for dishonored payments (an increase from $100 to $1,000 maximum penalty for single check/payment), and minimum penalty of $25 (up from $10).

Base Year Eligibility Changes: Amends Section 401(a) of the law to increase amount of base year wages that must be earned outside of highest quarter from 20% to 49.5%. Also, section 404(a) is amended to eliminate "third step-down" provision in benefits table, and instead make it two.

Change in Effective Date of Variable Claim Duration: Amends Section 404 of the law to state that the total amount of benefits claimants can receive is their weekly benefit rate multiplied by the number of qualifying credit weeks that they had (although it must be a minimum of 18), up to a maximum of 26 weeks. Moves the effective date from January 1, 2015 to January 1, 2013.

Limitations on Annual Maximum Compensation Increases: Section 404 ("Rate and Amount of Compensation") is amended to extend, through 2019, the current one year freeze on the maximum weekly benefit rate (frozen at $573). Starting in 2020 through 2023, the annual growth is then capped at 8% and the normal growth rate resumed in 2023.

Unemployment Compensation Solvency Bonds: The legislation amends the law to allow for the issuance of limited obligation revenue bonds through the PA Economic Development Financing Authority (PEDFA) if the Department of Labor and Industry determines that the issuance of bonds to repay federal unemployment compensation loans will result in a savings to employers in the Commonwealth.

The legislation will allow the department, with the approval of the Governor's Office of the Budget, to apply to PEDFA for funding for the repayment of federal loans and such funding will constitute a "project" for the purposes of PEDFA's enabling statute. PEDFA may issue bonds to finance a departmental request for federal loan repayment monies, and the total amount in bonds the department may request is $4.5 billion. Maximum term of the bonds shall not exceed 20 years. Bonds issued by the authority for purposes of federal loan repayment will not be a direct obligation of the Commonwealth and the full faith and credit of the Commonwealth is not pledged for the payment of principal or interest on any bonds issued for this purpose. The bonds will be secured by specific unemployment contributions (interest factor assessment revenue) and money that is in the Debt Service Fund.

Upon issuance of bonds, the proceeds shall be applied in the following order: 1) pay the costs associated with the issuance of the bonds; 2) fund bond reserves; 3) deposit in an appropriate fund monies to pay capitalized interest for a period not to exceed two years; 4) refund outstanding bonds; 5) make any other deposit required under any instrument or agreement pertaining to the bonds; 6) repay principal and interest of federal loans; and 7) deposit any balance into an unemployment compensation program fund relating to the bonds. The bond proceeds deposited in the unemployment compensation program fund shall be used to: 1) repay the principal and interest of the previous federal advances; 2) pay unemployment compensation benefits; 3) pay bond administrative expenses; 4) redeem or purchase outstanding bonds or pay bond obligations; and 5) pay bond obligations.

PEDFA must first give consideration to issuing the bonds by an open, public sale at not less than 98% of the principal amount and accrued interest to the highest bidder after public advertisement. If, in the judgment of the authority, a public sale will not produce the most benefit to employers and the Commonwealth, the authority shall adopt a resolution setting forth the details for the determination. A copy of the resolution would have to be transmitted to the Governor, and the Chairman of the House and Senate Labor and Industry Committees. The authority could then pursue a public negotiated sale.

A separate account is established in the State Treasury to be known as the "Debt Service Fund". The interest rate assessment collected for purposes of bond debt payment are to be deposited into the fund. The monies in the fund will be used for the following purposes, in priority order: 1) payment of bond obligations and bond administrative expenses, replenishment of bond reserves, and for redemption or purchase of outstanding bonds; 2) payment of annual federal loan interest obligations; 3) repayment of outstanding federal loan interest; and 4) transfer to the Unemployment Compensation Trust Fund if bonds and loans are paid off.

For each calendar year in which the bond obligations and administrative expenses are due, PEDFA must notify the department of the amount of bond administrative expenses so the department can determine the amount of assessment required for that year for deposit into the Debt Service Fund. If there is a deficiency in the Debt Service Fund, that part of principal owed on bonds may be paid from the Unemployment Compensation Fund.

Establishment of Re-employment Fund: Section 601.5 ("Reemployment Fund") is added into the law to establish the "Reemployment Fund" which will be a restricted revenue account within the State Treasury. The purpose of the fund will be to promote programs and services to assist individuals to become employed, and fund research/studies/technology upgrades to improve the department's ability to provide employment services. The monies that are deposited in fund annually must be expended or obligated for expenditure by June 30 of following year, or they will revert back to the Unemployment Compensation Trust Fund. The department is required to issue a report to the Governor/General Assembly by June 30th describing the activities provided by the fund during previous calendar year

The legislation amends Section 301.4 (Contributions by Employees") to allocate 5% of the employee unemployment tax to the Reemployment Fund from 2013-2017.

Increase in Statute of Limitations: Section 804 ("Recovery and Recoupment of Compensation") is amended to increase the statute of limitation from 6 years to 10 years for the collection of fault overpayments. The amendment of Section 804 shall apply to benefit years that begin on or after the effective date of the section, which is effective immediately.

Unemployment Compensation Amnesty Program: The legislation amends the law to establish the "Unemployment Compensation Amnesty Program". The program will exist for a period of three consecutive calendar months designated by the department which start no later than 360 days after the effective date of the act.

The amnesty program will apply to: 1) unpaid employer contributions through the first quarter of 2012; 2) unpaid reimbursements due on or before April 30, 2012; and 3) unpaid interest due on contributions through the first quarter of 2012, or on reimbursements due on or before April 30, 2012; and 4) unpaid penalties for reports filed late through the first quarter of 2012.

The amnesty program will also apply to: 1) a fault overpayment of compensation determined before June 30, 2012; 2) a non-fault overpayment determined before June 30, 2012; 3) fault overpayment for weeks before June 30, 2012 for which a determination has not been issued, but claimant acknowledges; and 4) unpaid interest on overpayments that were repaid on or before June 30, 2012.

During the amnesty period, an employer or employee will have to file an amnesty form containing all information required by the department. The employer/claimant must include the required payment along with the application. With respect to unpaid contributions, employers must pay all unpaid contributions/reimbursements/interest/penalties, lien filing costs (if applicable), and one-half of the interest and penalties due. Claimants must pay the outstanding balance of all fault overpayments, lien filing costs (if applicable), and one-half of the interest due. For non-fault overpayments, claimants must pay 50% of the outstanding balance of a non-fault overpayment. With respect to unpaid interest, claimants must pay one-half of any interest due and all of the lien filing costs (if applicable).

If a payment agreement exists between the department and an employer or claimant, the employer or claimant may participate in the amnesty program notwithstanding any terms of the agreements to the contrary. It also provides that Labor and Industry shall not commence any administrative or judicial proceedings against an employer or claimant participating in the amnesty program unless the liability was understated.

The department must establish guidelines to implement the amnesty provisions and publish the guidelines in the PA Bulletin no less than 90 days prior to the commencement of the amnesty period. Labor and Industry shall publicize the amnesty program and notify all employers and claimants who are known to have liabilities that are eligible for the amnesty program.

Required Reports: The legislation requires the department to submit to the Majority/Minority Chairman of the House and Senate Labor and Industry committees an annual report detailing all data on bonds issued and other relevant data for the previous year; the report would have to be submitted by March 1st each year.

In addition, the department must submit to the Majority/Minority Chairman of the House and Senate Labor and Industry committees a report detailing data/info on tax amnesty program; this report will have to be submitted with 240 days after end of amnesty period.

FISCAL IMPACT: According to the Department of Labor and Industry this legislation would save the Unemployment Compensation Trust Fund $375,000,000 in calendar year 2013. Assuming half would be saved in FY 2012-13 equals $187,500,000. The Department indicates the transfer to the Reemployment Fund would equal $10,000,000 in calendar year 2013. Assuming half would be transferred in FY 2012-13 equals $5,000,000. This legislation would save the Unemployment Compensation Trust Fund $2,312,000,000 (about $330,000,000 annually) over the next 7 calendar years.

The Department of Labor and Industry estimates that it will have to apply to PEDFA for the issuance of $3.37 billion to pay off federal loan advances by November 1, 2012. Issuing $3.37 billion in bonds at 2.75% (assumed true interest cost) would require debt service payments of $3.9 billion (about $390 million/year) over a 10-year period beginning in 2013 (based on level debt service payment methodology and no capitalized interest). Based on current economic predictions, employers are projected to pay $4.125 billion in additional interest assessments and Federal Unemployment Tax Act increases from 2012 through 2022. Assuming this scenario, employers would save a total of about $225 million from 2013 through 2022 or about $22.5 million per year.

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Estimates are calculated using the best information available. Actual costs and revenue impact incurred may vary from estimates.