

Statement  
Of  
Douglas J. Holmes  
President, UWC – Strategic Services on Unemployment and  
Workers’ Compensation and the National Foundation for  
Unemployment Compensation and Workers’ Compensation

June 25, 2021

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President  
UWC – Strategic Services on Unemployment & Workers’ Compensation and  
National Foundation for Unemployment Compensation and Workers’ Compensation  
[holmesd@uwcstrategy.org](mailto:holmesd@uwcstrategy.org)

Senator Jehlen, Representative Cutler and members of the commission, thank you for the opportunity to submit this statement with respect to Massachusetts unemployment trust fund solvency.

I am Douglas J. Holmes, President of the National Foundation for Unemployment Compensation and Workers' Compensation, a research foundation that annually publishes comparisons of state unemployment compensation laws and hosts the National Unemployment Insurance Issues conference.

I also serve as President of UWC Strategic Services on Unemployment & Workers' Compensation (UWC), the national membership organization serving as the voice of business specifically with respect to unemployment insurance (UI). UWC and its predecessor organization have served the business community in analysis of unemployment insurance policy since 1933. UWC members include a broad base of national and state business organizations as well as individual employers with specific interest in unemployment insurance.

I am pleased to be able to submit this statement to the Commission. I supervised staff and/or served in the role of Secretary of the Ohio Unemployment Compensation Advisory Council (UCAC) for more than 20 years. During that period, the UCAC effectively recommended UI related legislation that was enacted in every legislative session.

To provide a frame of reference, it is important at the outset to restate the purpose of UI and the Federal/State Employment Security System. This system is an employer financed insurance system designed to provide temporary, partial wage replacement for individuals who have become unemployed through no fault of their own in connection with work. As a condition of being paid unemployment compensation individuals must be able to work, available to work and actively seeking work. The system provides insurance against the risk of loss of wages due to unemployment, assists individuals as they seek employment, assists employers in hiring employees, and provides a counter cyclical stabilizer for the economy. The system is not designed or financed to guarantee a particular income or to entitle individuals to be paid unemployment compensation if they do not meet the requirements of the program.

Employers broadly support UI and the Employment Security system to provide a temporary safety net for employees who become unemployed through no fault of their own in connection with work. Employers also expect that the system will be efficiently run with integrity, trust funds will be managed effectively, and the program will provide timely partial wage replacement and avoid improper payments, fraud, and identity theft.

### Historical Background

Unemployment Insurance was initially established in 1935 under the Social Security Act as a program that covered only private sector employees. The program structure is somewhat unique in that it combines the imposition of a Federal Unemployment Tax (FUTA) to be paid by employers to produce revenue dedicated to fund administration of the state programs. The

rate of FUTA tax is adjusted with offset credits for employers in states in which state law meets conformity and compliance provisions of federal law. State UI trust fund accounts are managed by the U.S Treasury.

States have the responsibility to set state UI contribution rates and to determine benefit eligibility through methods of administration within general requirements of the federal grant of administrative funds.

The program as it was initially established has been expanded over the decades through a series of amendments, including expanded required coverage of employees of federal and state governments and non-profit entities (with certain limited exceptions), and extended unemployment compensation under certain circumstances of higher unemployment rates.

The U.S. Treasury manages each state unemployment insurance account as well as FUTA financed accounts that authorize the payment of federal funds for state administration (Employment Security Administration Account) Extended Benefits (Extended Unemployment Compensation Account) and the maintenance of an account through which states may seek advances to pay unemployment compensation (Federal Unemployment Account).

Massachusetts is one of eighteen states and the Virgin Islands with currently outstanding federal loans through the Federal Unemployment Account [https://www.treasurydirect.gov/govt/reports/tfmp/tfmp\\_advactivitiesched.htm](https://www.treasurydirect.gov/govt/reports/tfmp/tfmp_advactivitiesched.htm) . The primary reason for insolvency of these accounts in 2020 and 2021 has been the recession triggered by the COVID-19 pandemic and government mandated shutdowns.

I reviewed the status of the Massachusetts UI trust fund and the provisions of Massachusetts law and have the following observations and recommendations for your consideration as you develop measures to achieve long term solvency of the state UI Trust fund. Some of these measures have already been addressed with the enactment of H 90.

1. Secure federal funding from money available through the CARES Act and the American Rescue Plan Act (ARPA) to restore the UI trust fund balance to its pre-pandemic level on January 27, 2020.
2. Credit CARES and ARPA funds to the state account that is the basis for determining the solvency tax and to the employer accounts to which the payments of COVID-19 related payments were charged. Note that with respect to reimbursing employer accounts the crediting should take into consideration the federal credits already provided under Section 2103 of the CARES Act as amended.
3. To the extent that CARES and ARPA deposits are not sufficient to assure a solvent trust fund balance, use bond proceeds to be deposited into the state Special Contribution Unemployment Compensation Trust Fund that was recently established.
4. Develop unemployment trust fund projections to first establish a base line of the trust fund balance, tax rates, benefits, and other significant factors under current law.
5. Once there is agreement on the base line projections evaluate options to improve and maintain unemployment trust fund solvency.
6. Establish debt service assessments that result in employer costs which are less than the costs that would otherwise be imposed if the state were to rely on federal advances and repayment through FUTA offset credit reductions.

7. Closely monitor the status of the Special Fund and the general trust fund and exercise options to pay off the outstanding bond obligations early if the economy improves faster than anticipated.
8. Include a review of other state experiences in the implementation of alternative financing. Texas has a history of authorizing bonds and adjusting debt service amounts and paying off early. Also, US DOL has published a review of state alternative financing that is a reference for best practices.

In addition to these basic procedural recommendations, there are a number of current provisions in the Massachusetts UI law that should be reviewed for amendment as part of a long-term solvency package.

### **1. Taxable Wage Base and UI Contribution Rates**

The taxable wage base should be evaluated in combination with the rate schedule to determine the cost per employee for employers under UI law in comparison to other states. The comparison should also evaluate the cost per employee by industry and address the rates for new employers, minimum contribution rates, average contribution rates, and maximum contribution rates. This evaluation should be a reference as the state considers modifications to address solvency with an understating of the impact on employer cost and whether employers in Massachusetts are paying more or less in contributions than employers in other states with which Massachusetts may compete for economic development.

A snapshot of the distribution of the tax burden among employers in Massachusetts should be developed and the impact of changes over time should be tracked to assess tax burden as a percentage of payroll. Rate schedules and tax bases are not starting from zero, and any modifications should not produce spikes in cost that are so great as to discourage employers from hiring employees.

### **2. Consider reducing the time before employers are eligible for experience rating.**

The Massachusetts requirement of three years is longer than the requirement in most states. A longer period of assigned contribution rate may result in an average experience rate for the state that is lower or higher than the overall experience with unemployment claims that would otherwise result. A one-year requirement would be consistent with federal law and the laws in many states.

### **3. Set the general new employer rate at 1.0% to encourage economic development and set the new employer rate for the construction industry at the average contribution rate for employers in the construction industry.**

Federal law requires a new employer rate of at least 1.0% until there is sufficient experience on which to base an experience rate. A 1.0% new employer rate will encourage employer start ups and could be combined with a new employer rate for construction set at the industry average to avoid out of state competitors for in state contractors.

### **4. Cap the Solvency Tax and Review the charging of benefits to the solvency account.**

Many states have accounts to which benefits may be charged when benefits are not chargeable to individual accounts but cap the solvency tax to be assessed based on the balance in these accounts to avoid spikes in solvency taxes. There also may be charges to the account that should instead be charged to individual employer accounts.

The recent experience with the solvency tax rate may be repeated after future recessions and a cap could avoid the spike that would otherwise be imposed.

## **5. General Observations for Review**

### **a. Massachusetts is among the states with the highest unemployment tax burden for employers.**

The cost as a percentage of total wages as of 2020 in Massachusetts was among the highest in the country.

Connecticut	0.78%
Florida	0.12%
Maine	0.57%
Massachusetts	0.82%
New Hampshire	0.16%
New York	0.41%
Rhode Island	1.09%
Texas	0.39%
US	0.49%

The higher cost of unemployment taxes in Massachusetts puts the state at a competitive disadvantage with other states and world markets in attracting new employers and retaining businesses.

In addition to the negative impact on economic development, the higher UI tax burden makes it more difficult for small business in Massachusetts to survive and discourages employers from taking the risk of hiring additional employees.

Unless there is significant growth in the tax base for UI through the addition of new workers in the state, the cost of unemployment benefits will go up for employers unless there is a change in the benefit determination formula and/or significant integrity measures to reduce benefit pay out. Higher benefits paid with reduced payroll drives the benefit ratio up and increases experience rated taxes.

The best solution to insolvency is economic growth that increases the overall tax base at the same time that it reduces the unemployment compensation pay out.

It should be noted that many states (including Connecticut, New York, and Texas) have recently enacted UI solvency legislation that should be reviewed for an updated comparison.

**b. Massachusetts is among the states with the highest average weekly benefit amounts and highest maximum weekly benefit amounts in the country.**

A comparison of average maximum weekly wages as of the 4<sup>th</sup> quarter of 2020, shows:

Average WBA	
Connecticut	\$332.59
Florida	\$227.69
Maine	\$312.02
Massachusetts	\$468.09
New Hampshire	\$281.71
New York	\$343.17
Rhode Island	\$336.71
Texas	\$393.09
US	\$327.04

Maximum WBA in Selected surrounding states as of 2020

Connecticut	\$649 - 724 with dependents
Massachusetts	\$823 - 1234 with dependents
New York	\$405
Rhode Island	\$586 - 732 with dependents

To accurately evaluate wage replacement, a review of the weekly benefits paid to individuals who file for unemployment in comparison to their own base period wages is needed. The averages published by US DOL do not evaluate the wage replacement as compared to an employee's base period wages, and a state study of this data would be helpful in determining the distribution of wage replacement percentages within the claimant population.

**c. The formula to determine the WBA in Massachusetts increases wage replacement and may discourage return to work.**

The weekly benefit determination formula uses a high quarter review that increases the weekly benefit amount. A percentage of base period average weekly wage would reduce WBAs but retain a meaningful wage replacement with reference to the base period.

**d. The size of the Massachusetts outstanding debt is too great to overcome in a short period of time.**

Permitting the FUTA tax to go up automatically, is not an equitable way to address solvency, and it also takes too long to generate the revenue needed to pay off the outstanding debt. The automatic FUTA tax increases also end when the debt is paid and would not assist in the building of adequate positive reserves before the next recession.

Since the 2008-2009 recession many states with large outstanding loans have carefully developed legislation to address solvency with models to project costs and projection tools to

estimate short- and long-term costs and benefits of alternatives. The US Department of Labor provides a forecasting model free of charge and provides training for state employment security agency staff in its use. Private models are also available that include more complete analyses of the drivers of cost in individual state UI laws and administration.

In addition, for many possible statutory modifications, estimates may be developed from labor market information, wage information and/or benefit information available in state systems. A five percent sample of claims, for example, may be used to project the impact of changes in the benefit formula.

## **6. Benefit and Integrity Suggestions**

### **a. Change the Weekly Benefit Amount (WBA) calculation to 1/52 of base period wages.**

The formula currently used to determine the weekly benefit amount in Massachusetts results in higher weekly benefit amounts for seasonal workers and higher weekly benefits than most states in the country. The law computes the weekly benefit amount using the highest two quarters in the claimant's base period. This methodology can result in claimants being discouraged from accepting work available off season that may pay less than the weekly benefit amount.

Many states compute the weekly benefit amount based on the average of wages in the entire base period in order to align the WBA to be paid during the benefit year with the similar twelve-month period prior to application for benefits.

### **b. Eliminate the dependency add-on.**

Only 13 states have dependency provisions. No additional federal funding is provided for administration of dependency provisions, and the addition to the weekly benefit amount pushes the potential weekly benefit amount in Massachusetts to the highest weekly benefit amount in the country.

UI is designed as a partial wage replacement for each individual worker and is not a household support program. Today it is common to have multiple wage earners in the same household. It becomes administratively burdensome to sort out the number of dependents and whether the dependents may be claimed by one wage earner or another.

A modification to eliminate the provision, reduce the payment and/or simplify the determination of dependency could reduce administrative expense and cost to the trust fund while maintaining wage replacement percentages for the majority of claimants. Elimination or simplification of the dependency provision could also result in a reduction in the percentage of claims deemed to be improperly paid.

### **c. Change the earnings disregard from 1 & 1/3 times the basic WBA to 20% of the WBA.**

The current disregard is higher than other states and results in increased payout and a reduced differential between working full time and drawing benefits with earnings disregard.

**d. Limit total benefits payable to a percentage of base period wages**

Many states have total benefits payable limitations so that the amount of UI benefits does not exceed a percent of wages paid during the applicant's base period.

**e. Make a refusal of suitable work a duration suspension until the individual removes the suspension through subsequent work instead of just a suspension of benefits for a specified number of weeks.**

Most states treat refusals as duration suspensions.

**f. Require that applicants must have their identities verified BEFORE establishing benefit eligibility and make the payment of weekly claims for benefits subject to independent work search verification (not "self-certification").**

The experience with the COVID-19 recession has demonstrated the need for increased attention to applications and to verification of identity. This is not only a basic integrity issue but becomes a trust fund solvency issue when there is organized crime attacking the UI benefit payment process.

**g. Freeze the maximum weekly benefit amount at current levels until the UI trust fund balance reaches solvency.**

Obviously, the automatic increase in WBA is a major cost driver for insolvency and temporary maximum weekly benefit freezes are typically used to address insolvency. By freezing the maximum weekly benefit amount the workers with lower income will not be affected and the impact on higher wage earners will be relatively minor and temporary.

**h. Reduce the number of potential weeks of unemployment compensation.**

Although many states have laws providing for up to 26 weeks of unemployment compensation, many states also have provisions for lesser numbers of potential weeks for individuals with minimal base period earnings. Some states after the 2008-2009 reduced the number of potential weeks of benefits and temporarily increased them to 26 due to the COVID-19. The potential number of weeks of benefits should be evaluated as part of long-term solvency considerations. As a practical matter, most claimants do not normally exhaust all of the weeks potentially available because they return to work. The goal of the employment security system is to assist individuals in returning to work.

There is no federal requirement that a state provide 26 or more weeks of unemployment compensation, and a reduced number of potential weeks would reduce benefit payout. It should also be noted, however, that the number of weeks available may impact the number of weeks of extended unemployment compensation under the applicable federal law.



## **Conclusion**

The overall goal of solvency should be implemented through a plan to achieve an adequate positive balance and/or triggered measures to assure that the state avoids having to borrow to pay state unemployment compensation. The plan should be implemented over a period of years and include ongoing monitoring to assure that solvency is maintained.

Econometric models should be used to project the impact of each proposed change along with assumptions with respect to the unemployment rate, benefit pay out, and revenue from taxes.

A plan that relies solely on tax increases to achieve solvency under the current circumstances would require increases so great as to place Massachusetts at a competitive disadvantage with neighboring states and the country as a whole. A plan that relies solely on benefit cuts would reduce the value of the UI safety net for those who become unemployed.

In designing a plan, tax and/or benefit measures should be phased in to assure effective implementation and to avoid significant spikes in taxes and/or large cuts in benefits as much as possible while meeting solvency goals.