

Commission on Unemployment Compensation
August 9, 2010
Richmond, Virginia

The Commission on Unemployment Compensation met on August 9, 2010, in Richmond, Virginia, with Chairman John Watkins presiding. John Broadway, who became Commissioner of the Virginia Employment Commission (VEC) about 90 days earlier, briefed the members on the status of the Unemployment Trust Fund and related issues.

EMPLOYMENT DATA

The Commonwealth's unemployment rate for June 2010 was 7.3 percent. Last June, the rate was 6.6 percent. Virginia's unemployment rate for months in 2010 has averaged about 10 percent higher than rates for the same months in 2009. The Commonwealth's unemployment rate in this recession peaked at 7.8 percent in February of this year, which was the highest rate in Virginia since it reached 8.1 percent in February 1983.

The growth in the number of unemployed Virginians has increased the VEC's workload. The annual number of initial claims has grown from 260,561 in 2007 to 501,950 in 2009. The number of initial claims for unemployment benefits for the first six months of this year is 204,320. This figure shows a promising reduction from the same period last year when 271,600 initial claims were filed. The decline of almost 25 percent was attributed to fewer layoffs related to the motor vehicle, furniture, retail, building and financial sectors.

First payments of unemployment insurance benefits from January through June 2010 are 28.6 percent less than in the corresponding period in 2009 but 44.6 percent higher than in the corresponding period in 2008. The average duration for receipt of unemployment benefits was 16.7 weeks in June 2010; for the same month of 2009, the average duration was 13.5 weeks. Final payments of benefits in the first six months of 2010 are up 4.6 percent from the same period in 2009 and up 149.1 percent from the same period in 2008. The exhaustion rate, which reflects the percentage of unemployment compensation recipients who use up all of the weeks of regular unemployment benefits for which they are eligible, was 51.7 percent in June 2010; in the same month of 2009 it was 51.5 percent.

Virginia's maximum weekly unemployment benefit is \$378; the national average is \$400. The maximum weekly benefit reflects a weekly benefit replacement rate of 42.6 percent of the state's average weekly wage. In 2009, the same maximum weekly unemployment benefit amount provided a weekly benefit replacement rate of 43 percent.

UNEMPLOYMENT TRUST FUND

The Unemployment Trust Fund is funded by state unemployment taxes, which are paid by employers at a rate that varies depending on the solvency level of the Trust Fund and each employer's claims experience. The balance in the Unemployment Trust Fund on January 1, 2009, was \$546.7 million. On January 1, 2010, the balance was negative \$122.4 million, which included a \$62.8 million Incentive Distribution from the federal government. The balance is

projected to fall to negative \$341.8 million at the end of 2010. While disappointing, this year's figures are not as bad as those that had been projected. Last summer the Trust Fund balance was expected to fall to negative \$194.2 million on January 1, 2010, and to negative \$561.4 million at the end of 2010. State unemployment tax revenue is projected to rise from \$327.7 in 2009 to \$516.1 million in 2010, while interest revenue will fall from \$13.9 million to zero. The amount of unemployment compensation benefits paid in 2009 was almost \$1.074 billion; it is projected to fall to around \$735 million this year.

The solvency level of the Trust Fund is calculated by dividing its balance on June 30 by an amount, determined in accordance with a statutory formula, that represents an adequate balance. The Unemployment Trust Fund's solvency level on June 30, 2008, was 64 percent, and on June 30, 2009, was 24.4 percent. Mr. Broadway reported that the solvency level is projected to have been negative 12.8 percent on June 30, 2010, which is an improvement over the negative 20 percent that had been projected a year ago. The solvency level of the Trust Fund is projected to be about negative 10 percent in June 2011, and then return to a positive balance of about seven percent in June 2012, 30 percent in June 2013, and 52 percent in June 2014. Reaching a solvency level of 50 percent in 2014, starting the next calendar year, will end the Social Security benefit offset and the imposition of the fund builder tax of 0.2 percent of the first \$8,000 of each employee's wages.

Title XII of the federal Social Security Act provides a mechanism by which states may borrow funds to offset shortfalls in their unemployment trust funds. During the current recession, 33 states and the Virgin Islands have borrowed from the Federal Unemployment Account. Until this recession, Virginia has borrowed to meet its unemployment obligations once. In April 1983, the Commonwealth borrowed \$45 million, which was repaid by September of that year. The prompt repayment allowed Virginia to avoid liability for interest on the loan.

The current recession has required Virginia to borrow for a second time. Since October 2009, the Commonwealth has borrowed from the federal government in order to pay unemployment benefits. The balance owed as of July 27, 2010, was \$347 million. Virginia has not made such borrowings from the federal government since April 2010, though another loan may be required before the end of the calendar year. The VEC anticipates that Virginia will borrow an additional \$838 million through April 2013.

Borrowing from the federal government has several substantial implications. States are required to pay interest on the federal loans in 2011 (though the 2009 federal stimulus legislation waived interest on such loans to states for 2010). Legislation has been introduced in Congress to waive states' obligation to pay interest in 2011; its fate is uncertain. If the waiver of interest is not extended beyond 2010, Virginia will be required to pay interest of \$20.2 million in 2011 and 2012. Interest payments cannot be paid from the Trust Fund or federal grants, and are expected to be made from state general funds. Members of the Commission urged the VEC Commissioner to work to have the administration include funding for the federal interest obligations in the amendments to the biennial budget to be considered during the 2011 Session.

Failing to repay the borrowed federal funds has substantial implications. Currently, most employers pay federal unemployment tax (FUTA) at a rate of 0.8 percent of each employee's

first \$7,000 of wages, for a cost of \$56 per employee per year. This figure reflects the FUTA tax credit of 5.4 percent, which reduces the rate from 6.2 percent to 0.8 percent. However, employers in a state with an outstanding loan balance in two consecutive years will lose 0.3 percent of the 5.4 percent credit. This will raise employers' tax rate from 0.8 percent to 1.1 percent of the first \$7,000 of each employee's wages, which increases the annual FUTA liability for each employee by \$21, from \$ 56 to \$77. If this increase takes effect, the increased FUTA receipts will be applied to the state's loan balance, which in Virginia's case will reduce the balance by \$85 million in January 2012. Moreover, for each year beyond the two that a state has a loan balance, the FUTA tax credit is reduced by an additional 0.3 percent, resulting in a further tax liability of \$21 per employee.

A factor contributing to rising state unemployment tax (SUTA) assessments is the increasing number of business failures, which has increased the number of unemployment benefit payments charged to the pool rather than to an active employer's account. This is expected to increase the pool tax assessed against remaining employers from its 2010 level of \$22 per employee to about \$48 in 2012. The pool tax rate for 2010 is 0.28 percent. Employers are also assessed with a 0.20 percent fund builder tax.

The low level of solvency of the Trust Fund automatically increases the SUTA rate assessed on employers. The program's counter-cyclical funding formula links higher tax rates to low Trust Fund solvency rates. At the Trust Fund's current level, employers are taxed under the highest of the 15 existing tax tables. The average annual state unemployment tax per employee assessed on employers in Virginia, exclusive of the FUTA assessment, was \$96 for the fiscal year ending September 30, 2009. The corresponding national average was \$259.94. However, the VEC projected that the average annual SUTA assessment per employee will rise to approximately \$160 in 2010, \$200 in 2011, and \$225 in 2012.

When the pool tax and fund builder tax are included, the average state tax per employee is \$161.60. The minimum tax, paid by 112,000 employers, is \$46.40, and the maximum tax, paid by 11,000 employers, is \$534.40.

EMERGENCY AND EXTENDED BENEFITS PROGRAMS

Virginia's unemployment compensation program provides a maximum of 26 weeks of regular benefits. The federal government has enacted, and the General Assembly has amended its laws to permit, emergency unemployment benefits programs. The Tier I emergency benefits program provides for up to 20 extra weeks of benefits, and the Tier II program allows up to 13 weeks, plus one week added in November 2009, of benefits in "high unemployment states," defined as those with an unemployment rate exceeding six percent. Those who have exhausted Tier II benefits and extended benefits are eligible in high unemployment states for 13 weeks of Tier III benefits. If a state's unemployment rate equals or exceeds 8.5 percent, Tier IV benefits can provide another seven weeks of benefits.

The extended benefits program provides up to 13 weeks of benefits for claimants who have exhausted their regular benefits and Tier I and Tier II emergency benefits, and is available in states that have certain levels of unemployment. The extended benefits program includes

enhanced job search requirements. In February 2009, Congress increased the federal share of such extended benefits to 100 percent. Another seven weeks of extended benefits are available at a state's option to claimants in states when unemployment exceeds 8.5 percent.

As a result, unemployed Virginians may be eligible for a maximum of 86 weeks of benefits. Of these, 26 weeks are financed through the State's Unemployment Trust Fund and the balance is funded by federal appropriations. Additional seven weeks of benefits may become available in Virginia if the unemployment rate exceeds a certain levels.

The VEC's report prompted questions regarding prospects for improvements. Mr. Broadway noted that there is some good news, including the fact that though Virginia had anticipated borrowing \$1.2 billion from the federal government, currently it anticipates borrowing only \$960 million. In addition, the rate of jobs creation this year was calculated to be the third highest in the nation. The Governor had announced in July that the Commonwealth has added 71,500 jobs since February. VEC data provided at the meeting states that between June 2009 and June 2010, Virginia's nonfarm employment increased by 1,500 jobs. The apparent discrepancy was explained as reflecting the seasonal changes, and well as not accounting for job losses between June 2009 and January 2010.

2010 UNEMPLOYMENT COMPENSATION LEGISLATION

Staff provided the Commission with an overview of legislation pertaining to unemployment compensation that was introduced during the 2010 Session. Of the two bills that passed, one (House Bill 535) postponed the scheduled increase, from \$2,700 to \$3,000, in the minimum amount of wages an employee must have earned in the two highest earnings quarters of his base period in order to be eligible for unemployment benefits. The other, House Bill 550, authorizes the VEC to negotiate the terms of repayment for benefits to which a recipient is not entitled, deduct up to 50 percent of future benefits, or forego collection of the payable amount until the recipient has found employment.

Two items of legislation, House Bill 252 and House Joint Resolution 49, also dealt with the issue of overpayments of unemployment compensation benefits occurring due to an administrative error by the VEC. These items were carried over to the 2011 Session, and are being examined by the Auditor of Public Accounts as part of its audit of the VEC. The Auditor's report is expected to be completed by the fall. This Commission intends to revisit the issue when the Auditor's report is completed.

Of the roughly half dozen items of legislation that did not pass during the 2010 Session, most dealt either with the eligibility of seasonal employees for unemployment benefits or attempts to expand eligibility for unemployment benefits in order to make Virginia eligible for federal stimulus funds.

HOUSE JOINT RESOLUTION 23: DEPUTY-LEVEL HEARINGS

Delegate R.G. Marshall introduced House Joint Resolution 23 in the 2010 Session. The measure was tabled in the House Commerce and Labor Committee, and the Chair asked this Commission to examine the issue.

The resolution would have directed the Joint Legislative Audit and Review Commission to study the effectiveness of deputy-level hearings on claims under the Virginia Unemployment Compensation Act. The resolution recites that it is appropriate to determine the rate at which decisions at the deputy level approving benefits claims are overturned and whether the reasons for the rate of reversals on appeal indicate a failure of decision makers at the deputy level properly to interpret and to implement the applicable provisions of the Virginia Unemployment Compensation Act.

After speaking briefly to his purpose for introducing the resolution, Delegate Marshall introduced John Milhiser, the owner of several small businesses in Northern Virginia. Mr. Milhiser described his concerns with deputy-level hearings. He described four cases where a former employee sought benefits, he contested the person's eligibility, the claimant was found after a deputy-level hearing to be eligible, and the deputy's decision granting benefits was overturned on appeal. While he ultimately prevailed in each case, Mr. Milhiser objected to the expenditure of time and money that was required, particularly when the same evidence was provided at both levels of hearing. His criticisms focused on a perceived cultural bias that favored claimants, which is expressed in such actions as coaching claimants about their testimony. He recommended improved training and education for hearing examiners as a means of addressing the bias issue.

The VEC's Chief Administrative Law Judge, Coleman Walsh, provided the Commission with an overview of claims adjudications by the VEC's deputies. He noted that the agency began reviewing and evaluating the claims adjudication process prior to the introduction of House Joint Resolution 23. The review was prompted by a sharp increase in the number of claims adjudicated by the VEC. The agency has launched a comprehensive self-study focusing on organizational design, business processes and workflow, staffing, training, and examining best practices from other states.

The VEC is expecting to complete an interim report this summer, and to have a final report by the fall. Judge Walsh was invited to present the final report to this Commission at its next meeting. The VEC's data indicates that approximately one quarter of claims decisions were reversed on appeal in 2008, with the percentage falling to 22.6 percent in 2009. When claims involving issues related to separation from employment are examined, the percentage overturned on appeals rose to 29.5 percent in 2008 and 28.8 percent in 2009.

While the data does not indicate why the decisions were reversed, Judge Walsh observed that in about half of cases one party does not participate at the initial hearing. When a case in which one side did not participate is heard de novo on appeal, a reversal is not surprising. A related reason for decisions being overturned on appeal involves situations where a third party presents a case on an employer's behalf before a deputy and is not aware of the specific facts surrounding an employee's separation. In such a case, the information that was not available at the first level of hearing may be provided when it is heard de novo at the second hearing. The members agreed

that the hearings should be unbiased and fair, and that perhaps an education program would be an appropriate response to the concerns identified by Mr. Milhiser. Delegate Morrissey requested the VEC to include in its report any specific statutory changes that it finds are appropriate to address shortcomings with the current system.

In closing, Delegate Purkey expressed concern that the federally funded extensions of unemployment benefits are being paid for with borrowed money, and he questioned how long we can use borrowed capital to pay benefits. He also asked the VEC to look at the issue of layoffs by state and local governments, which are required to reimburse the Unemployment Trust Fund for benefits paid to their eligible laid-off employees.

Chairman Watkins urged the members of the Commission to continue examining the burden on private employers of increasing levels of SUTA taxes and the loss of the FUTA credits. The Commission should continue its practice of looking at the tax levels and benefit levels in other states in the region.

FUTURE MEETING

The Commission will hold a meeting later in the year, at which the VEC will provide updates to its projections regarding the Trust Fund's solvency level. The meeting is also expected to receive the Auditor of Public Account's report on benefits overpayments due to administrative error and the VEC's report on the claims adjudication process.