WASS

Wisconsin Association of Staffing Services

American Staffing Association

April 15, 2013

Ms. Janell Knutson
Unemployment Insurance Advisory Council, Chair
Department of Workforce Development
201 East Washington Avenue, Room E300
Madison, WI 53708-8942

Strengthen Wisconsin's UI System and Equalize the UI Tax Burden:
Lower UI Tax Rates and Increase the Taxable Wage Base

Dear Chair Knutson,

The Wisconsin Association of Staffing Services ("WASS")[1] and its members are acutely aware of Wisconsin's ongoing depleted UI Trust Fund and the painful financial consequences to Wisconsin employers that have followed. While there are several opportunities to improve our UI system, we put forth a single proposal that we believe would have the greatest positive impact on the financial health of our UI system, make UI costs more predictable for Wisconsin employers, and ensure a more equitable tax treatment between different Wisconsin employers and industries.

Wisconsin employers currently pay Wisconsin unemployment taxes on the first $14,000 in wages each employee is paid each calendar year (the "taxable wage base") with a maximum tax rate of 9.8%. Tax rates are set largely based on an employer's UI claims relative to the SUTA taxes it pays. Compared to other states, Wisconsin has high SUTA tax rates and a low taxable wage base.[2]

How We Got Here. It is clear to see how Wisconsin's UI Trust Fund is where it is today. DWD Secretary Newson's "Financial Outlook" Report to the Governor and Legislature in January 2013 ("Secretary's Report") provides a clear explanation and ultimately cites two primary causes: (1) our taxable wage base was/is too low; and (2) the UI tax schedule change triggers are set too low.

The Secretary's Report concludes by noting that the UI Advisory Council and Legislature should advance solutions to the financing of our UI system that address the following objectives: (1) assure repayment of existing loans; (2) restore the UI Trust Fund to solvency; and (3) build and maintain sufficient reserves to meet the obligations of projected future benefit expenditures. This WASS

[1] In 2011, Wisconsin staffing companies employed 235,657 Wisconsin workers and generated $1.1 billion in payroll. 86,120 of those temporary employees bridged to permanent jobs. Source: U.S. Bureau of Labor Statistics and American Staffing Association.

[2] About 30% of states have a maximum rate of 5.4% on wages between $24,000 to $28,000. http://www.unemploymentinsurance.doleta.gov/unemploy/content/sigpros/2010-2019/January2012.pdf

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proposal addresses all of these objectives while also making the financing system more equitable between different Wisconsin employers and industries.

WASS Proposal: We propose increasing Wisconsin's taxable wage base and significantly decreasing Wisconsin's SUTA tax rates to levels that will ultimately be revenue neutral for the State, meaning there would be no net decrease in SUTA tax receipts. However, in light of the ongoing insolvency of the State's Trust Fund, we propose that the SUTA tax rates be only partially reduced until the Trust Fund regains solvency, at which time the rates can be fully reduced.

As shown by data below, recent experiences with the Great Recession and a comparison of how states with different tax rates and taxable wage bases have fared relative to Wisconsin fully support this change. We also believe that raising the taxable wage base to approximately $28,000 would make Wisconsin more attractive to many employers because SUTA tax rates could be significantly lowered. Although we do not have sufficient data and/or financial modeling tools available to propose a specific amount that SUTA tax rates should be lowered, the intent of this change is to ultimately lower SUTA rates in an amount sufficient to offset the additional revenue coming in from the higher taxable wage base. The overall change resulting from this proposal would be revenue neutral to the State after Trust Fund solvency has been restored.

> Example: Assuming the taxable wage base is increased to $28,000 and SUTA tax rates can be lowered on average approximately 2.5% under this proposal, this variation would lower SUTA tax rates only 1.5% on average until the Trust Fund is solvent at which time SUTA tax rates are lowered the remaining 1.0%.

Other Concepts for Strengthening UI Financing System

Indexed Wage Base. WASS also supports the concept of an indexed wage base (meaning the taxable wage base is tied to a state's total wages), as long as SUTA tax rates can be lowered in the process. An indexed wage base model allows the taxable wage base to fluctuate based on the health of a state's economy. Recent experience with the Great Recession demonstrates that indexation better positions a state to avoid insolvency and limits the degree of indebtedness in the event that the state does need to borrow. Only six of 16 indexed programs (38%) borrowed during 2009–2011 compared to 29 of 35 nonindexed programs (83%) during that period. For the six indexed states that did borrow, the average amount they borrowed was 0.55 percent of their total state payroll compared to 0.80 percent of payroll for the nonindexed states.[3] In 2012, the average taxable wage base in indexed states was $28,700 and just $10,682 in nonindexed states. Another significant benefit to indexation is that adjusting or increasing the taxable wage base would not require future legislative action.

A Note On Tax Rate Schedule Triggers. WASS understands that the responsiveness of our State's financing system could also potentially be improved by lowering the trigger levels of the State's tax schedules, but taking only that action: (1) does nothing to make our financing method more equitable

[3] Data from U.S. Department of Labor, Unemployment Insurance Financial Handbook (1960–2011).

between different employers; and (2) will not speed our ability to pay down our debt as Wisconsin has already been on its highest tax schedule ("Schedule A") for several years.

WASS Proposal Rationale

1. **A Higher Taxable Wage Base Will Provide Stronger & Broader UI Financial Footing, and Minimize the Likelihood of Higher FUTA Taxes and "Special Assessment" Payments**

Over time, the ability of a state's UI financing mechanism to produce sufficient revenue is greatly assisted by subjecting more of its wages to UI taxation. UI Trust Funds in states with higher taxable wage bases can recover from or avoid insolvency better than states with lower taxable wage bases. Having an ample UI Trust Fund is critical to minimizing the likelihood of Wisconsin employers being assessed an unplanned special assessment and/or paying more federal unemployment taxes (through a reduction in the FUTA credit). In 2011, Wisconsin employers paid an unexpected $42.3 million in "special assessment" payments ("SAFI"). In 2012, Wisconsin employers made an additional $35.8 million in SAFI payments. By law, Wisconsin had to use this assessment to pay the interest on the State's outstanding UI-related loan from the federal government. The DWD - UI Division forecasts that Wisconsin employers will have to pay a special assessment again in 2013 and 2014 for the same reason. The Secretary's Report estimates that the total amount of SAFI payments made by Wisconsin employers from 2011-2014 will be $105 million.

By virtue of the size and duration of the State's outstanding Trust Fund Loan balance, Wisconsin employers also paid an additional $46.7 million in FUTA taxes during 2012. The DWD - UI Division projects that Wisconsin employers will continue to pay higher FUTA rates in 2013 and may have to do so in 2014. The Secretary's Report estimates that the total loss of FUTA credit reductions to Wisconsin employers would end up costing between $275 and $500 million.

Key Point: With a larger Trust Fund balance and/or the ability to recover more quickly from the significant negative outflow of dollars from the UI system that occurred during the Great Recession, Wisconsin and its employers would have been in a much better position to avoid or significantly minimize these unexpected, additional UI-related tax payments. Had our financing system included a higher taxable wage base, one that more closely tracked the State's increase in total wages from 2000 to 2008, it is very likely that Wisconsin employers would have avoided much or all of the $275 - $500 million in lost FUTA credit reductions and the $105 million in SAFI payments. The time to lower SUTA tax rates and increase the taxable wage base is long overdue.

Employer UI Experiences in Other Midwestern States

As of April 10, 2013, the following data from Midwestern states demonstrates that UI Trust Funds in states with relatively higher taxable wage bases have weathered the increase in UI benefit payments during the Great Recession much better than those states, like Wisconsin, with lower taxable wage bases. Employers in those other states avoided costly FUTA credit reductions and/or unexpected special assessments.

	2013 Taxable Wage Base	Federal Loan Balance[4]	2012 FUTA Credit Reduction[5]	Employer Interest Paid FY '11 & '12[6]
North Dakota	$31,800			
Minnesota	$29,000			$ 18,167,471
Iowa	$26,000			
Wisconsin	$14,000[7]	$1,007,459,077	0.6 %[8]	$ 78,091,172
Missouri	$13,000	$ 569,249,474	0.6 %	$ 45,507,041
Illinois	$12,900	see footnote[9]		$119,813,817
Michigan	$ 9,500	see footnote[10]		$137,659,352
Indiana	$ 9,500	$1,793,031,980	0.9 %	$121,495,158
Ohio	$ 9,000	$1,920,604,892	0.6%	$136,543,342

Key Point: In short, states with higher taxable wage bases can recover from or avoid UI Trust Fund insolvency faster and more fully than states with lower taxable wage bases. Lowering SUTA tax rates and increasing the taxable wage base would decrease the likelihood of Wisconsin's Trust Fund reaching such a depleted state in the future – and avoid the significant additional tax payments paid by Wisconsin employers that follow in such situations.

4 As of April 10, 2013. http://www.workforcesecurity.doleta.gov/unemploy/budget.asp#tfloans.

5 http://www.workforcesecurity.doleta.gov/unemploy/finance.asp . Employers in a state with a FUTA credit reduction of 0.6% pay an additional $42 in FUTA taxes per worker with wages of $7,000 or more.

6 http://www.workforcesecurity.doleta.gov/unemploy/finance.asp

7 As of 2013. Wisconsin's taxable wage base was $12,000 in 2009 and 2010, and $13,000 in 2011 and 2012.

8 Wisconsin employers will face a larger FUTA credit reduction, of 0.9%, in 2013 if the state still has loan balance on November 10, 2013. Employers in a state with a FUTA credit reduction of 0.9% pay an additional $63 in FUTA taxes per worker with wages of $7,000 or more.

9 Illinois had a bond issue in 2012 to pay off its UI Trust Fund loan (balance of negative $2.1 billion).

10 Michigan had a bond issue in 2011 to pay off its UI Trust Fund loan (balance of negative $3.2 billion).

As the data above clearly demonstrates, states with a relatively low taxable wage base are experiencing or have recently experienced one or more of the following undesirable results: (1) a lingering Federal Trust Fund Loan balance; (2) a FUTA credit reduction (higher FUTA taxes for its employers); and/or (3) significant interest paid to the federal government (often in the form of "special assessments" paid by its employers).

2. UI Tax Burden Should be Shared More Equitably Between Different WI Employers

Under Wisconsin's current UI tax financing system, some employers pay significantly less taxes for the same amount of payroll than other employers do – even when those groups have the same exact tax rate. Businesses in the restaurant, hospitality, tourism, agricultural, retail and temporary staffing industries tend to employ more part-time employees, seasonal employees and short-term employees. As a result, employers with a large base of these workers currently pay a disproportionately high amount of UI taxes.

> Illustration – Status Quo. To illustrate the disparate burden of the current formula on many Wisconsin employers, assume that two Wisconsin employers, a professional services firm (Employer A) and a restaurant (Employer B), have the same WI SUTA tax rate (4%) and the same amount of total annual payroll ($1 million).
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> If Employer A has 10 employees who each earn $100,000 in wages, that employer will pay $5,600 in Wisconsin SUTA taxes each year. If Employer B has 100 employees who each earn $10,000 in wages, that employer will pay $40,000 in Wisconsin SUTA taxes each year – or **more than 7 times more in SUTA taxes** than the professional services firm - even though each employer has the same SUTA tax rate and the same amount of payroll dollars. Under the current Wisconsin model, Employer A has paid Wisconsin unemployment taxes on 14% of its payroll and Employer B has paid Wisconsin unemployment taxes on 100% of its payroll.[11]
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> Illustration – Using Proposed Lower SUTA Rates and Higher Taxable Wage Base. Using the same scenario above, and assuming SUTA rates were reduced by 1.5% to 2.5% and the taxable wage base was $28,000, Employer A would pay $7,000 in Wisconsin SUTA taxes and Employer B would pay $25,000. Employer B **would still pay 3.5 times more in SUTA taxes** than Employer A – despite identical SUTA tax rates and annual payroll amounts – but that difference would still represent a dramatic improvement from the status quo.

Lower SUTA tax rates and a higher taxable wage base distribute UI taxes more fairly between different employers and industries, reducing the current disproportionately high tax load on employers with relatively more part-time, seasonal or lower-wage employees.

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[11] Employer A pays Wisconsin UI taxes as follows: $14,000 x 10 employees = $140,000 of wages subjected to unemployment taxes on a total of $1,000,000 in payroll. Employer B pays Wisconsin UI taxes as follows: $10,000 x 100 employees = $1,000,000 of wages subjected to unemployment taxes on a total of $1,000,000 in payroll.

3. **A Higher Taxable Wage Base Makes An Employer's SUTA Tax Rate More Relevant**

The financing of our federal and state UI systems are based on an experience-rated model. In short, experience-rated models ensure that employers with less favorable experience (more claims relative to taxes paid) pay a higher tax rate. This feature of our system makes sense. However, the lower the taxable wage base, the less important an employer's SUTA tax rate becomes – since that rate is applied to a smaller proportion of the employer's total payroll. By increasing the taxable wage base, Wisconsin employers would be more fairly held to account for their UI experience (whether positive or negative).

4. **Lowering Wisconsin's UI Tax Rates Will Attract & Retain More Employers**

Wisconsin's "new employer" SUTA tax rate is currently the 9th highest among all states and Wisconsin's maximum SUTA tax rate is currently the 11th highest among all states.[12] While employers consider a variety of cost factors when deciding where to locate, SUTA tax rates are usually among those carefully reviewed. Generally speaking, more attention is paid to tax rates than to taxable wage base levels. Increasing the taxable wage base will allow the State to lower SUTA tax rates – and make Wisconsin more attractive to new businesses relative to other states.

In conclusion, the time has come to revisit the way in which Wisconsin finances our UI system. This WASS proposal will: (1) assure repayment of existing loans; (2) restore the UI Trust Fund to solvency; and (3) build and maintain sufficient reserves to meet the obligations of projected future benefit expenditures. Our proposal also lessens the long-standing disparate UI tax burden between different Wisconsin employers and industries. We appreciate the UI Advisory Council's consideration of this proposal and its many related issues. If the Council would like any additional information, including testimony on any of the information presented in this letter, please feel free to contact me directly.

Sincerely,

Lori A. Malett

Lori Malett
President, Hatch Staffing
Wisconsin Association of Staffing Services (WASS), Board President

12 http://www.unemploymentinsurance.doleta.gov/unemploy/content/sigpros/2010-2019/January2012.pdf