Overview of Unemployment Insurance Claim and Tax Process

Joint Legislative Task Force on
Unemployment Insurance Benefit Equity

June 29, 2005

Introduction

- UI program created in the federal Social Security Act of 1935.
- Federal/state program, with incentives for states to adopt conforming state UI programs.

SUTA and FUTA

- Employers pay both state UI tax and federal UI tax (FUTA).
  - State UI tax paid to state and revenues held in the state's UI trust fund.
  - FUTA paid to IRS and revenue held in the federal UI trust fund.

Conformity

- What are the incentives for state’s UI programs to “conform?”
  - Tax credit
  - Program funding

Conformity – Tax Credits

- FUTA tax rate is 6.2% on first $7,000 of employee’s wages.

- Tax credit: Employers in states with “conforming” programs pay 0.8%.

Conformity – Program Funds

- States with “conforming” UI programs receive federal funds from FUTA revenue for program administration.

Flow of FUTA Funds

FUTA 0.8% of $7,000 Tax Ceiling

Administrative Funding

Excess Amounts

Extended Benefits

Excess Amounts

Loan Fund

Excess Amounts

Reed Act Account

Congressional Appropriations

Distributions to States
$8 Billion March 2002

Examples of Conformity Issues

- Use of $$ in state UI trust fund to pay benefits.
- Minimum taxable wage base.
- Tax rate of 5.4%, unless reduced on the basis of the employer's experience.
- Minimum new employer rate of 1%.
- Pay full FUTA rate of 6.2% for any state-exempted employee covered by federal law.

Examples of Conformity Issues

- Nonprofit and public sector coverage
  - Nonprofits may elect reimbursing or taxable.
  - State agencies are reimbursing.
  - Local governments may elect reimbursing or a special tax system.
- Reimbursing employers v. taxable employers

Case Study

Case Study

- The Employer has no claims, and therefore, pays contributions in the lowest rate class.

- The Employer hires an employee, but then lays off the employee the following year.

- Chart – Row 1 and Row 2.

Case Study

- The Employee files a claim for unemployment benefits.

- The Employee receives a monetary determination and a claimant handbook.

- Chart – Row 3.

Case Study

- The <u>Separating Employer</u> receives a notice of the claim.

- The <u>Base Year Employer(s)</u> also receives a notice of the claim.

Case Study

- The Employee files weekly claims and begins receiving benefits.
- The Employee claims her maximum benefits.
- Chart – Row 3.

Case Study

- The Employer:
  - Receives a quarterly notice of benefit charges;
  - Files a quarterly tax report; and
  - Receives an annual tax rate notice.
- Chart – Row 4 and Row 5.

Case Study

- The Employer continues to:
  - Receive quarterly notices of benefit charges;
  - File quarterly tax reports and pay taxes; and
  - Receive employer tax rate notices for 2007.

- Chart – Row 6, Row 7, and Row 8.

History

History - Benefits

- Before 1977: Benefits were 1/25 (4 percent) of wages in high quarter.
- 1977: Benefits were 4% of average of wages in 2 high quarters.
- 1978: 680 hours of work required to qualify.

History - Benefits

- 2004: Benefits were 4% of wages in average of 3 high quarters.
- 2005 (from January 2 to April 23): Benefits were 1% of base year wages.
- 2005 (for two years): Benefits are 3.85% of wages in average of 2 high quarters.

History - Taxes

- Before 1985: Flat rate tax of 3%, not experience-rated. (Experience-rated system could – but did not – trigger on.)
- 1984 (effective 1985): New tax system with multiple tax schedules, based on 4 years of experience, an indexed taxable wage base, and a maximum rate of 5.4%.

History - Taxes

- 2003 (fully effective by 2005): New tax system with one tax schedule and a maximum rate of 6.5% (with exceptions).

- 2005 (effective for two years): Temporary tax changes for certain employers.