Senate Fiscal Agency
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BILL ANALYSIS

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Senate Bill 500 (Substitute S-1 as passed by the Senate)
Sponsor: Senator Ken Horn
Committee: Economic Development and International Investment

Date Completed: 10-13-15

RATIONALE

The Michigan Employment Security Act establishes the Unemployment Compensation Fund, which is used to pay unemployment benefits when due, and is funded by employer contributions. The amount of an employer's contribution to the Fund is determined by multiplying the employer's unemployment tax rate (a percentage based on various factors, such as the employer's history of benefit charges) by a "taxable wage limit" (or base) for each covered employee. Under amendments enacted in 2011, the taxable wage limit is set at $9,500 but may be lowered to $9,000 depending on the Fund balance. That is, if the Fund balance is at or above $2.5 billion, the rate decreases to $9,000 for nondelinquent employers; but if the balance is below $2.5 billion, the rate is increased to $9,500. The calculation must be made for each calendar quarter, based on projections of the Fund balance made by the Unemployment Insurance Agency (UIA). On July 30, 2015, the UIA announced that the taxable wage limit would be reduced to $9,000 beginning with third-quarter tax filings in October.

Some people believe that the current structure of determining the taxable wage limit quarterly could be confusing to employers if their unemployment taxes were to change throughout the year. Additionally, there is concern that the current structure could create uncertainty and unnecessary operational costs if the rate fluctuated frequently. To address these concerns, it has been suggested that the taxable wage limit should be determined annually.

CONTENT

The bill would amend the Michigan Employment Security Act to require an annual, rather than quarterly, determination of the balance of the Unemployment Compensation Fund, for the purpose of setting the taxable wage limit; provide for the determination to be based on the Fund's balance as of the previous June 30; and require the taxable wage limit to be reduced from $9,500 to $9,000 for the calendar year if the balance equaled or exceeded $2.5 billion on that date and were projected to remain at that level for the next quarter.

Currently, the taxable wage rate is $9,500 and calculated quarterly. If the balance in the Unemployment Compensation Fund at the beginning of a calendar quarter equals or exceeds $2.5 billion, however, and the Unemployment Insurance Agency projects that the balance will remain at or above that level for the remainder of the quarter and the entire next quarter, the taxable wage limit for that quarter and the next quarter will be $9,000 for an employer that is not delinquent in the payment of unemployment contributions, penalties, or interest.

Under the bill, starting in 2016, if on June 30 of the previous year the balance in the Unemployment Compensation Fund equaled or exceeded $2.5 billion and the UIA projected that the balance would remain at or above $2.5 billion for the following calendar quarter, the taxable wage limit for the calendar year would be reduced to $9,000 for a nondelinquent employer. If these conditions were not met, the taxable wage limit for the calendar year would be $9,500 for all employers.

For these purposes, if an employer had a quarterly unpaid balance of $25 or more, the employer would be considered delinquent unless one or more of the following applied:

-- The employer had filed a timely protest or appeal of the notice of assessment and the assessment had not become final.
-- Within 45 days after the beginning of the first calendar quarter in which the reduced taxable wage base limit took effect, all outstanding balances owed to the UIA were paid.
-- If the employer were a domestic employer, all applicable contributions, interest, and penalties were paid by the date specified by the UIA.

MCL 421.44

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument
Employers contributing to the Unemployment Compensation Fund could save money under the bill. Quarterly fluctuations in the taxable wage limit could affect the amount of unemployment taxes collected from employers. If the wage limit were set annually, however, there could be only one change to contributions for the year. If that change were a decrease, the employers could see the benefit of a decrease for a full year, instead of potentially seeing the benefit for a single quarter under the current Act. According to the UIA's July announcement, lowering the taxable wage limit from $9,000 to $9,500 means that about $16.0 million less in taxes will be assessed in 2015 and approximately $57.0 million less will be assessed in 2016, assuming the taxable wage limit stays at $9,000 throughout 2016.

Supporting Argument
The proposed structure would provide more stability and certainty for businesses and the UIA. Businesses generally perform better in a predictable environment, and without the legislation to streamline the process, a "seesaw" effect could take place with rates going up and down, causing confusion and problems for employers.

Supporting Argument
Compared to current law, the proposed process for setting the taxable wage limit would be less burdensome, complicated, and challenging for the UIA and its workers. The current structure requires the UIA to notify employers if there are changes throughout the year. Quarterly changes also could require the Agency to reprogram its computers and recalculate employer contributions. The bill would alleviate these challenges and free-up Agency resources for other purposes.

Opposing Argument
The current Act allows for flexibility. If there is a situation that requires a raise in the base, the State can respond quickly with quarterly determinations. The proposed annual determinations would delay the State's ability to react to economic changes that could deplete the balance of the Unemployment Compensation Fund.

Response: There are existing safeguards to ensure that the Fund stays healthy. One safeguard is that the taxable wage limit is based on the current balance plus projections into the next few quarters. Economists use complex analytical tools that can help predict the economy over the next two quarters. These results are a factor in determining whether to raise or lower the base. Another safeguard is a three-year look-back period, rather than the previous five-year look-back period, for determining an employer's experience rating. This shorter period allows quicker adjustments to the amount of unemployment tax collected.

Opposing Argument
The current process for lowering employer contributions when the Fund is healthy appears to be based on the assumption that any extra money should go to the employer instead of the unemployed worker. By trying to streamline the process, the bill would reinforce this concept and

the practice of giving businesses tax cuts as opposed to helping the individuals who are unemployed through no fault of their own.

Response: The bill would not lower or cut the tax rate of businesses. Rather, it would just stabilize the taxable wage limit for businesses that contribute to the Fund. Under the Act, the limit can be either $9,500 or $9,000. Just as the bill would prevent the $9,000 limit from rising to $9,500 for a year, it would prevent the limit from being reduced from $9,500 to $9,000 for a year, if it returned to that level.

Legislative Analyst: Drew Krogulecki

FISCAL IMPACT

The bill would have no immediate fiscal impact on the State and no impact on local units of government. In the future, the bill could result in both positive and negative impacts on the Unemployment Compensation Fund. Currently, the Michigan taxable wage base is discounted to $9,000 because the Fund balance is at or above $2.5 billion. This means that there would be no impact on the Fund at this time.

Under current statute and practice, if the Fund balance falls below $2.5 billion in any quarter, the taxable wage base discount is removed and the base is increased to $9,500 in the next quarter. The State is able to respond quickly to drops below $2.5 billion and replenish the Fund at a rapid rate. Changing the taxable rate base only once a year would result in a slower response to drops in the Fund. This could result in a loss of up to $57.0 million for a full year of not increasing the taxable wage base. However, by allowing only one time annually when the taxable wage base can be increased, the bill could result in lower administrative costs to change the taxable base amount. Changing the wage base annually also could reduce the potential for employers' taxes to be delinquent, which may result from miscommunication about the changes to the base.

Currently, the Unemployment Insurance Agency allows employers that file a timely protest to be considered not delinquent as a standard practice, which the bill would put into statute. The UIA also already considers an employer not delinquent if all contributions, interest, and penalties are paid by the date specified by the Agency. These amendments would not result in a cost to the Agency, because they would not change current practice. Under the only new change, if an employer paid all contributions, interest, and penalties by the middle of the first calendar quarter, the employer's taxable wage base could be reduced to $9,000 for the remainder of the year. This would result in minor administrative changes within the Agency and costs, but those costs could be covered under current appropriations. The amendment also could give employers an incentive to pay delinquent contributions, interest, and penalties at a faster rate.

Fiscal Analyst: Cory Savino