



North Carolina UI Solvency Study Observations and Recommendations

MAY 18, 2012

Commissioned by:



EMPLOYERS COALITION OF NORTH CAROLINA



Prepared for North Carolina Chamber Foundation and ECNC by:



Authors:

Antonio C. Fiore, Attorney, Kegler, Brown, Hill & Ritter
Douglas J. Holmes, President, National Foundation for Unemployment Compensation & Workers' Compensation
Jim Hemmerly, Consultant
Thomas Whitaker, Attorney and Consultant

Table of Contents

I.	Background on the Authors.....	3
II.	Executive Summary.....	5
III.	Background on Economy and Impact on UI System.....	8
IV.	Overview of the North Carolina UI System.....	9
V.	North Carolina Solvency and UI Debt Review.....	12
	a. National Unemployment Trust Fund Solvency Map.....	13
	b. UI Debt Repayment Recommendations.....	15
	c. Bond Recommendations.....	15
VI.	Reemployment and Workforce Training/Education.....	18
	a. Reemployment and Workforce Training/Education Recommendations...21	
VII.	Integrity of the UI System.....	25
	a. Integrity Recommendations.....	25
VIII.	Affordability/Benefits.....	31
	a. Affordability/Benefit Recommendations.....	32
IX.	Taxes.....	45
	a. Tax Recommendations.....	46
X.	Administrative Recommendations.....	49
XI.	Overall Impact of Recommendations.....	50

I. Biographical Information on Authors

Antonio C. Fiore, Attorney – Of Counsel Kegler, Brown, Hill & Ritter, LPA



Antonio C. Fiore, Esq. serves as Of Counsel for Kegler, Brown, Hill & Ritter. Mr. Fiore previously served as the Director of Labor and Human Resources Policy for the Ohio Chamber of Commerce for 10 years as the lead lobbyist for all labor and employment issues, including unemployment compensation. During his tenure, Mr. Fiore worked with state UI agency officials and lawmakers to simplify Ohio's unemployment compensation laws and help advocate for increased support for the state's workforce development and reemployment services. In this capacity, Mr. Fiore testified in the Ohio House of Representatives Commerce & Labor Committee as well as the Ohio Senate Insurance, Commerce & Labor Committee. He also served as the Ohio Chamber's liaison to the U.S. Chamber of Commerce's Labor Relations Committee. Mr. Fiore also served as the Chamber's lead spokesperson for print, radio and television media inquiries for labor and human resource issues.

He has been actively engaged in unemployment and employment security issues for over a decade focusing most of his work in the last four years on state-by-state tracking of legislative changes related to the American Recovery and Reinvestment Act of 2009 and state UI trust fund solvency. Mr. Fiore has tracked and reported on UI legislation as well as significant law changes in all 50 states for the Washington, D.C. based organization UWC since 2008. Mr. Fiore is a 1998 graduate of the Max M. Fisher College of Business with a Bachelor of Science in Business Administration majoring in International Business. He also received his Juris Doctorate from Capital University Law School in 2004.

Douglas J. Holmes, President UWC Strategy, Inc. – Strategic Services on Unemployment & Workers' Compensation



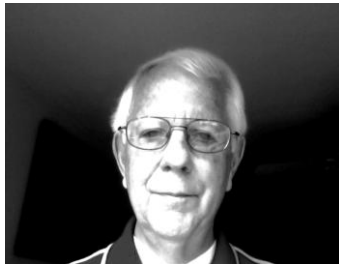
Douglas J. Holmes began as President of UWC in November, 2006. In his position as President of UWC, Doug serves as the primary UI legislative and policy resource for business, counting as members an array of national and state business trade associations, Fortune 500 companies and third party administrators. He also serves as President of the National Foundation for Unemployment Compensation & Workers' Compensation, which produces regular comparisons of state UI law and hosts the annual national unemployment insurance issues conference. Doug joined UWC after more than 22 years in positions in the public sector in which he developed policy and administered the federal/state unemployment insurance system.

During his tenure in state government, Mr. Holmes served as Deputy Administrator of the Ohio Bureau of Employment Services, Deputy Director of the Ohio Department of Job and Family Services, Ohio Unemployment Insurance Director, Chief Counsel for Unemployment Insurance, and Secretary of the Ohio Unemployment Compensation Advisory Council appointed by the Governor.

North Carolina UI Solvency Study Observations & Recommendations

In addition to his work in Ohio, Mr. Holmes served as Chairman of the UI/ES Reform Workgroup for the National Governors' Association, coordinator of the Coalition for Employment Security Financing Reform, and a member of the US Department of Labor UI Reform Workgroup. He has been a frequent speaker on the topic of the unemployment insurance system before Congress, state legislatures, state and national business organizations, state agencies, and labor organizations. UWC has served as the coordinator of a broad based UI business coalition seeking relief from federal unemployment taxes and advocating for improved integrity of the UI system. Mr. Holmes is an Attorney, and graduate of the Ohio State University and the University of Toledo College Of Law.

Jim Hemmerly **Consultant**



Mr. Hemmerly has a long and distinguished career in the Ohio agency with oversight of the state's unemployment system. He dedicated most of his career at the Ohio Bureau of Employment Services from 1970 to 1998. During that time he worked within the Labor Market Information Division from 1970 to 1990, and was the Assistant Director from 1983 to 1990. He continued his state service as the UC Advisory Council Secretary within the UC Special Programs Department from 1990 to 1998. He retired from state service in October 1998.

Since then Mr. Hemmerly has continued his public service at the Washington-Centerville Public Library from 1999 to 2007 where he served in various roles. He retired March 2007. He began his public service career in the US Army from 1968 to 1970 and was honorably discharged as SP5E5 August 1968. Mr. Hemmerly received his Bachelor of Science in Economics from The Ohio State University (OSU) in 1968. He also received his Master's in Business Administration from OSU in 1976. He also completed a substantial amount of work toward a Doctorate of Philosophy in Labor and Human Resources at OSU.

Tom Whitaker **Attorney and Consultant**



Thomas Whitaker is an Attorney and Consultant in Raleigh, N.C. Previously, he worked for the N.C. Employment Security Commission (ESC) in legal, legislative and managerial positions and was named Acting Chairman in 2000. He retired in 2010 after serving for 4 years as Deputy Chairman and General Counsel. During his 36 years with the ESC, he frequently testified before the N.C. House and Senate Committees concerning unemployment insurance legislative and trust fund issues. Mr. Whitaker represented the ESC before Federal and N.C. Courts and appeared before the N.C. Supreme Court in unemployment insurance and employment cases.

In 2000, Mr. Whitaker was named the "2000 State Administrator of the Year" by the National Association of Workplace Professionals and in 2003 he chaired a five year review of the unemployment insurance benefits systems for all states. Mr. Whitaker served as President of the National Association of State Workplace Agencies (NASWA) in 2008 and in that capacity testified before a Congressional House sub-committee and the Senate Finance Committee concerning unemployment insurance and workforce issues. He served as Chair of the NASWA Unemployment Insurance Committee in 1999 and 2003. Mr. Whitaker received his Juris Doctorate from Wake Forest University in 1974 and attended the National Judicial College.

II. Executive Summary

The purpose of this comprehensive solvency study is to recommend ways to help return North Carolina's unemployment insurance (UI) Trust Fund to a position of solvency now and assure continued solvency into the future. A solvent UI trust fund serves to strengthen the state's position in an increasingly competitive global marketplace. The study describes a balanced approach, with shared sacrifice and opportunity for unemployed workers and for employers seeking to not only survive, but to thrive. The study describes ways in which the state may encourage faster reemployment and allow for a common sense administrative structure which promotes continuous improvement in returning UI claimants to work more effectively while also improving the supply of qualified applicants referred to fill the needs of North Carolina employers.

The study includes a review of North Carolina's current state of UI solvency and a comparison to other states with respect to the benefits paid to claimants, taxes paid by employers, integrity measures, and general delivery system. We found that benefit levels and unemployment taxes were higher than in surrounding states, the outstanding federal debt was among the highest in the country, many of the best practices in integrity measures had not yet been implemented, and there was a need to address systems development and integration between local offices, call centers and one-stops to improve UI adjudication and to assist unemployed workers with reemployment and employers in finding the skilled workers that are needed. We developed recommendations with respect to improved administration, legislation and policy in each of these areas.

It is important to note that none of the changes contained in this study affect existing benefits being paid to unemployed individuals. It should also be noted that no change will interrupt the payment of unemployment benefits to eligible UI claimants. Timing is of critical importance in reviewing the changes recommended in this document. Particular attention should be given to the additional costs that will be levied on North Carolina employers if steps are not taken in 2012 to address the issues facing the UI system. Finally, by far the most critical observation of this study is that anything less than making the comprehensive reforms will only produce marginal results and likely lead to a series of ongoing reforms or "Band-Aids" in attempt to fix the current UI system. This document is largely based off the premise that asking employers to continuously pay more for a system that they fully fund without greater oversight and continuous improvement is simply unsustainable.

Solvency and UI Debt

North Carolina's unemployment insurance system is running an annual deficit of approximately \$470 million (see page 11 for analysis). This deficit has led to the current UI debt to the federal government of \$2.4 Billion placing it 4th highest in the country. The state would significantly improve its solvency position by repayment of the debt quickly to avoid future FUTA tax increases on employers, and additional interest payments. Taking no action will result in a series of increases in the rates to be paid by employers under the Federal Unemployment Tax Act (FUTA). The FUTA tax increases triggered under federal law will increase as long as the state continues to have outstanding debt until reaching \$420 per employee instead of the \$42 per employee due under the base FUTA rates. Increases will be greater on a percentage basis for employers with the lowest state UI experience rates. In addition to automatically increasing FUTA taxes, federal law requires that states pay interest on outstanding loans and repayment of interest must be made from sources other than the state UI tax. The costs of failing to immediately address UI Solvency are significant in the

form of increased federal unemployment taxes that increase each year that the outstanding loan is not repaid and interest charges to be paid by the state. A range of recommendations, including state UI tax increases; unemployment benefit cuts and refinancing the debt are recommended. Adding a bond package to eliminate the outstanding debt would move NC from a deficit state to a state without debt with a balanced fund and slowly building a positive balance and a reserve. The UI Trust fund should be restored to a healthy and solvent position for long-term sustainability and to be prepared for future economic downturns.

Re-Employment and Workforce Training/Education

States across the country have begun to turn the focus of UI systems to reemployment, and North Carolina is in a position to adopt the best practices from other states in the development of a set of performance measures and a delivery system that may serve as a model. There is currently \$1.4 Billion budgeted for workforce development programs throughout the state. Improvements and integration of systems are needed to focus on reemployment through performance based standards. Such measures should focus on individuals actually getting jobs rather than the completion of a program by the individual. Employment should be given greater weight when determining the success of workforce development and adult education and training programs whether funded by the federal, state or local government. Employment should not be the only metric used to determine if publicly funded resources are being utilized in the most effective manner. Retention rates are also critically important in determining if education and training programs are meeting the needs of North Carolina employers as well as jobseekers. Employing UI claimants, whether in permanent full-time jobs or part-time jobs while they complete an education or training program, helps replenish the UI Trust Fund by reducing benefit pay-out and increasing unemployment tax revenue. In addition to UI tax revenue, employment saves the state in reduced payout for public assistance and support payments while increasing state income tax revenue and increasing spendable cash to bolster the local economy.

Integrity

North Carolina and many other states during and after the 2008-2009 recession opted to dedicate limited administrative resources to the payment of benefits to the exploding number of unemployed workers. One result has been an increase in the number of overpayments and a lesser emphasis on integrity in benefit determinations, identification of fraud and overpayments, and the collection of overpayment amounts. Improvements must be made to the system in assuring that claimants are in fact qualified and eligible to be paid benefits and returning the focus of the program to assisting unemployed workers in their efforts to get back to work. Establishing and enforcing new requirements for claimants to be able, available and actively seeking work should be a focal point in reforms to the system. In North Carolina, UI claimants are only required to make two employer contacts per week as a requirement to continue to receive benefits. The documentation and verification of work search requirements have been de-emphasized in many states in recent years with the advent of internet claims, increases in claims load, and the priority placed by USDOL on making UI benefit payments quickly. Best practice states have implemented required registration for work and the required development by claimants of work search plans as conditions of eligibility for payment. Increased requirements in these areas will not only result in reductions in benefit overpayments, but will also reduce the duration of claims and send the signal to claimants that they are expected to be actively seeking work. In addition, improved staff training on rules, regulations and laws, is needed to bring objectivity to the system and improve consistency statewide in decision making.

Affordability/Benefits

Benefit payout has outstripped the ability to pay for the UI program. The benefit payout overhang in many states has continued longer than previous recessions due to the lack of significant job growth and the continuation of benefit payment provisions. A number of states across the country have taken action to reduce benefit payout through the reduction of the potential number of weeks of benefits, changes in the determination of the weekly benefit amount, and requiring a waiting week. Unemployment Compensation payments in North Carolina have exceeded unemployment tax revenue due to a number of factors, including: (1) the weekly benefit amount formula used to determine the amount to be paid results in amounts that are close to the national average, but significantly higher than the weekly benefit amounts in the region; (2) the maximum weekly benefit amount is significantly higher than maximum weekly benefit amounts in the region; and (3) wage replacement rates are higher than the national average and significantly higher than wage replacement rates in the region. Significant reductions in benefit amount and/or duration will be needed to eliminate the annual deficit in benefit payments compared to contributions and to reduce the current UI trust fund deficit. In addition, ensuring the benefit structure is competitive with other states and provides the right incentives for returning people to work is of critical importance. A conservative estimate of the impact of the recommended changes to the North Carolina UI system is projected to be an annual savings of over \$400 million.

Taxes

North Carolina employers *fully fund* the state's unemployment insurance program and pay over \$1.1 Billion in annual state UI tax. Employees make no contribution into the unemployment trust fund. The average per employee state UI taxes paid by employers in North Carolina is higher than other states in the region, however, the current tax rates do not generate sufficient revenue to cover benefits on an annual basis or to build solvency in the UI trust fund. Amendments to the current tax rates are needed to assure that the state UI tax structure is responsive to changes in the economy and capable of providing adequate funds to pay state UI benefit amounts over a reasonable time period as needed without borrowing from federal accounts. Tax rate schedules should provide improved experience rating as the basis for rates with reduced rates for low unemployment experience employers in North Carolina. UI Tax rates should be set so as to enable North Carolina employers to compete with employers in other states and in the global marketplace. Tax rates that result in increases in costs discourage job creation and result in a shrinking tax base. Recommendations in this study proscribe a balanced approach to address UI solvency and encourage job creation in North Carolina, and changing the minimum tax rates to distribute the cost of the UI system more completely across the full range of unemployment experience.

A piecemeal approach to addressing the needs of North Carolina employers, UI claimants and jobseekers will not produce as successful a result as implementing the complete package of reforms. The primary stakeholders in the UI system, legislative leadership in both houses and the Governor's office should be continually updated with respect to UI trust fund solvency to enable the state to take action in a timely manner.