

Approved: 2/15/96 ba
Date

MINUTES OF THE HOUSE COMMITTEE ON BUSINESS, COMMERCE & LABOR.

The meeting was called to order by Chairman Al Lane at 10:05 a.m. on February 9, 1996 in Room 526-S of the Capitol.

All members were present except: Rep. Barbara Ballard - excused
Rep. Vaughn Flora - excused
Rep. Jill Grant - excused
Rep. Candy Ruff - excused

Committee staff present: Jerry Donaldson, Legislative Research Department
Bob Nugent, Revisor of Statutes
Bev Adams, Committee Secretary

Conferees appearing before the committee: Bob Nugent, Revisor of Statutes
Jackie Summerson, Manpower

Others attending: See attached list

Briefing on:

HB 2540 - Establishes benefit ratio contribution system for unemployment tax

Bob Nugent, Revisor, explained to the committee that **HB 2540** changes the contribution method for unemployment tax from the reserve ratio to the benefit ratio system. Experience rating is the variation in employment security tax rates in relation to an individual employer's experience with unemployment. The goals of experience rating are: 1) to encourage employers to stabilize their employment; 2) to encourage employers to take active interest in the system; and 3) to provide an adequate fund balance. Two systems are used by most of our states, the reserve ratio and benefit ratio contribution system. Thirty two states including Kansas use the reserve ratio formula. Fifteen states use the benefit ratio system of experience rating. (see Attachment 1)

Mr. Nugent ended his briefing on the bill by answering questions from the committee.

Jackie Summerson, Manpower Temporary Services, appeared before the committee to further brief the committee on **HB 2540**. She was involved with the drafting of the bill. She and her husband are owners and operators of twenty-nine Manpower offices in Kansas and Missouri. They have a lot of payroll. Unemployment insurance is a huge expense to them every year but their benefit charges are fairly low. That disparity is what prompted her to investigate methods of experience rating used in other states. She explained that the changes proposed in the bill could not take place as long as the moratorium on unemployment taxes is in effect. The change could only take place when the moratorium ends. It would not cause a tax increase. The benefit ratio system as proposed does not collect any more or less unemployment taxes than the current system. It also does not have any effect on benefits paid to workers. She explained the different types of formulas used for experience ratings. She also gave some comparisons of the systems used by other states. The benefit ratio method of determining employer contribution rates basically makes the employers who are taking money out of the system pay more and the employers who are not taking money out of the system pay less. (see Attachment 2)

Mrs. Summerson ended her briefing on the bill by answering questions from the committee.

One concern brought up by Mrs. Summerson and committee members is the possible need to amend the bill to require a surcharge for employers with high benefit ratios.

Rep. Packer requested checking into the possibility of having the Director involved with unemployment contributions from the State of Iowa speak to the committee on that state's change to the benefit ratio contribution system.

Chairman Lane closed the briefing on **HB 2540** and the meeting was adjourned at 11:05 a.m.

The next meeting is scheduled for February 13, 1996.

HOUSE BUSINESS, COMMERCE & LABOR COMMITTEE
GUEST LIST

DATE February 9, 1996

NAME	REPRESENTING
Bill Lyles	KS. Dept. Human Resources
Tom McClure	- - -
Judith Ham	- - -
JASON PITTSBERGER	BRAD SMOOT
JANET STUBBS	KBIA
ART STROWER	MID AMERICA CORP
Jamie Clover Adams	KS Fertilizer and Chemical Assn
Dick Gibson	Jostens Printing & Publishing
Juli Summerson	Manpower
Jeff Chanay	Entz & Chanay

MEMORANDUM

To: The Special Committee on Labor and Industry
From: Robert J. Nugent, Asst. Revisor of Statutes
Date: 9-25-95

EXPERIENCE RATING: PURPOSES AND APPROACHES

I. Overview

Experience rating is the variation in employment security tax rates in relation to an individual employer's experience with unemployment. Experience rating exists in some form in every state employment security law and allows employers to take advantage of the federal 5.4% unemployment tax credit. Without experience rating, all employers would be charged a single uniform rate without advantage of the credit. The goals of experience rating are threefold:

1. to encourage employers to stabilize their employment;
2. to encourage employers to take active interest in the system; and
3. to provide an adequate fund balance.

Stabilization of Employment

The original purpose of experience rating was to provide incentives to employers to stabilize their employment. By increasing the rate of contributions proportionally to benefit charges incurred, employers are encouraged to avoid short-term layoffs by stabilizing production schedules. Furthermore, in theory, employers will be encouraged to avoid undesirable employment practices that would cause a voluntary quit situation chargeable to the employer.

This policy goal has been criticized for three reasons. First, the employer's ability to stabilize employment is controlled in large measure by outside forces such as change of season or changes in technology. Therefore, low rates are awarded not on the basis of good management, but upon good fortune.

Second, experience rating subsidizes employers by providing no interest loans to pay for benefits. An employer's rates do not increase until some period of time after it has incurred increased benefit charges. Thus it is able to pay for its increased benefits charges at a rate reduced by

*House Business, Commerce
& Labor Committee
2/9/96
Attachment 1*

inflation and offset by other the experience of other firms in its rate group. Studies conducted in the late 1970s concluded that employers pay roughly \$0.75 on the dollar for UI benefits. This has had the effect of encouraging short term layoffs. This is especially true of employers paying the highest rates. When an employer is paying the federal maximum rate of 5.4 percent or, in Kansas, an employer is at the top of the reserve ratio array, additional layoffs do not result in higher marginal rates. Therefore, experience rating has no effect on an employer already paying maximum rates except to the extent that an employer may hope to eventually escape the maximum rate group. For firms which experience seasonal or technology driven unemployment rates, experience rating is the least significant.

Finally, experience rating forces employers experiencing relatively low unemployment to subsidize employers with high or maximum rates. For an employer at the top of the reserve ratio array or paying the maximum rate, marginal changes in employment have no effect on rates. Even if the employer continues to experience high levels of unemployment, the rates charged the employer do not increase much since they are already at or near the maximum. To make up for additional costs due to increased benefit payments other employers are required to pay more taxes to insure that the fund balance is adequate. Nationwide, it is estimated that negative balance employers, (employers who withdraw more in benefits than they make in contributions), account for about 60% of benefit charges while paying only about 15% of total contributions. Thus experience rating, depending upon the scheme employed is unfair to employers who have achieved stable employment in the sense that the benefit costs of high turnover firms are socialized throughout the system. Overall, although experience rating does create a certain amount of unfairness, empirical studies conducted in the 1930s and 1960s both confirm that experience rating has resulted in a measurable increase in employment stability.

Encouraging Active Interest in the System

Another policy goal of experience rating is to encourage employers to take active interest in the system. By increasing rates based upon benefit experience, employers are encouraged to actively take measures to reduce benefit payments. This creates a private enforcement system by

encouraging employers to combat illegitimate claims and thereby reduce their rates.

This policy goal has been criticized as encouraging litigation and driving up administrative costs. At least one state has proposed creating a base benefit system to offset litigation costs. A base benefit would be an amount charged an employer's account for an employee separation. The charge would never be greater than the base amount regardless of the duration of the unemployment or the wage level of the employee. Furthermore, the employer is only charged for one base benefit per employee per year regardless of whether the employee is subsequently rehired by the same employer and then discharged again. In theory, by limiting the exposure of the employer in this manner, the incentive to litigate all but the most egregious claims is diminished. Such a proposal would have to be carefully considered in light of fiscal concerns and possible reduction in employer vigilance in denying bogus claims. No state has adopted such a proposal to date.

Maintaining Adequate Fund Balance

Experience rating acts as a safeguard to preserve adequate fund balances. When the economy is in recession and the drain on the fund balance is relatively high, experience rating increases rates by factoring in the high demand for benefits experienced in the past. Thus the fund is replenished by these increased rates and an adequate fund balance is maintained. Conversely, when the economy is relatively strong, rates decline in future because employers' experience indicates low demand for benefits. Thus experience rating should theoretically preserve an adequate fund balance at all times.

Our experience in Kansas demonstrates that this is not always true. Severe downturns in the economy can lead to depletion of the fund before increased future contributions can replenish it. Furthermore, prolonged periods of wage growth combined with relatively high employment can lead to very large fund balances.

II. FORMS OF EXPERIENCE RATING

Nationwide, there are two dominant forms of experience rating: "benefit ratio" and "reserve ratio." These two forms of experience rating

are employed by all but three states. The earliest and most popular form of experience rating is the reserve ratio formula. Thirty two states including Kansas use this formula.

Reserve ratio is determined by calculating a firm's past tax contributions and subtracting UI benefits charged to the employer's account. The remainder is then divided by the firm's average taxable payroll over a period of years. Most states consider three to five years of past payroll. Kansas considers three years.

Benefit ratio experience rating is employed in 15 states and is calculated by dividing total benefits charged to an employer's account over a period of three to five years and dividing that sum by the employer's taxable payroll over a similar period. No benefit ratio state considers less than three years or more than five years past experience with benefit charges and taxable payroll.

III. Comparison Of The Benefit And Reserve Ratio Systems.

There are two main differences between reserve ratio and benefit ratio systems. The first difference is that the benefit ratio formula does not account for a firm's past contributions. The only factors which affect a firm under a benefit ratio system are the growth or decline of both taxable payroll and charged benefits. Thus, since contributions are no longer considered the distinction between negative and positive account balance firms is eliminated.

The second primary difference between the two formulas is that the reserve ratio formula reflects a firm's total historical experience with benefit charges and contributions while the benefit ratio formula considers only the last three to five years of charged benefit experience. Therefore, a firm with a particularly high charged benefit year can be assured that after some period of time that benefit year will no longer be considered in the formula. Both formulas consider on a short period of average annual payroll.

Evaluating the two systems in light of the historical goals of experience rating reveals that the two systems are generally equal.

Stabilization of Employment

Since both systems raise rates for employers that experience high

levels of benefit charges, both systems provide the desired incentive to employers to lower their tax rates by stabilizing employment. Some of the criticism of experience rating generally is addressed switching to the benefit ratio system and some is addressed by remaining a reserve ratio state. As stated in the overview, experience rating is criticized because discharges are not always under the control of the employer, but are instead attributable to technological innovation or cyclical trends and it is unfair to penalize an employer for layoffs which he cannot stabilize. Benefit ratio, by discarding years of high benefit charges after a short number of years, is more forgiving of layoffs attributable to technological changes or long term changes in the business cycle.

With regard to the criticism that employers with relatively stable employment subsidize employers with unstable employment, reserve ratio can be viewed as superior to benefit ratio. In Kansas, an employer whose account balance is negative is charged the maximum allowable rate of 5.4 percent and is not eligible for the benefits of experience rating. Under a benefit ratio system this distinction would not apply. All employers would receive some level of experience rating and firms which formerly would have been paying the maximum rate of 5.4 percent might pay less than they do at present. Therefore, the criticism that experience rating creates an unfair subsidy is better addressed by the reserve ratio approach.

Active Participation by Employers

Both systems reward employers who are vigilant in taking steps to combat dubious unemployment compensation claims. Both systems factor in the amount of benefits charged to an employer and therefore reward employers who are able to avoid bogus claims. I could find no empirical evidence or scholarly opinion that would distinguish the relative incentives the two systems provide.

Fund Balance Stability

Both systems act to stabilize fund balance by requiring higher rates when benefit demand is high and lower rates when benefit demand is low. The reserve ratio system is better attuned to anticipating future demands for benefits. Higher levels of contributions are always a year behind higher demand for benefits, but by factoring in a firm's prior level of

contributions, the reserve ratio formula tends to better anticipate periods of high unemployment by building up fund balances prior to a recession. However, the benefit ratio can be more sensitive to changes in the economy because it is driven solely by recent changes in benefit demand. Levels of prior contributions which may not be related to the present state of the economy are ignored. The policy consideration is whether it is better to have a system that is quicker in adapting to changes in the economy or a system which provides more long term stability, but is less responsive to prevailing economic conditions.

IV. Conclusion

After reviewing the available empirical studies and legal articles concerning the relative merits of the two dominant forms of experience rating, a case could be made for either system. Both benefit ratio and reserve ratio accomplish the basic purposes of experience rating. However, the relative fairness of the two systems presents a series of policy questions for the committee.

1. To what degree should positive balance employers subsidize negative balance employers?
2. Should the experience rating formula favor historic employer experience or responsiveness to an employer's most recent economic condition?
3. Should the experience rating formula anticipate economic down turns or recover from them more quickly?

TAXATION

Table 200.--Summary of experience-rating provisions, 53 States ^{1/}

State	Type of experience rating				Taxable wage base above \$7,000 (41 ^{1/} States)	Wages include remuneration over \$7,000 if subject to FUTA (42 States)	Voluntary contributions permitted (24 States)
	Reserve ratio (33 States)	Benefit ratio (17 States)	Benefit wage ratio (2 States)	Payroll declines (1 State)			
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Ala.	• • •	X	• • •	• • • • • • • •	\$ 8,000	X	• • • • • • • •
Alaska	• • •	• •	• • •	Quarterly	\$23,900 ^{3/}	• • • • •	• • • • • • • •
Ariz.	X	• •	• • •	• • • • • • • •	• • • • • •	X	X
Ark.	X	• •	• • •	• • • • • • • •	\$ 9,000	X	X
Calif.	X	• •	• • •	• • • • • • • •	• • • • • •	• • • • •	X ^{2/}
Colo.	X	• •	• • •	• • • • • • • •	\$10,000	X	X
Conn.	• • •	X	• • •	• • • • • • • •	\$10,000	X ^{4/}	• • • • • • • •
Del.	• • •	• •	X	• • • • • • • •	\$ 8,500	X	• • • • • • • •
D.C.	X	• •	• • •	• • • • • • • •	\$10,000	X	• • • • • • • •
Fla.	• • •	X	• • •	• • • • • • • •	• • • • • •	X	• • • • • • • •
Ga.	X	• •	• • •	• • • • • • • •	\$ 8,500	X ^{4/}	• • • • • • • •
Hawaii	X	• •	• • •	• • • • • • • •	\$25,500 ^{3/}	X	• • • • • • • •
Idaho	X	• •	• • •	• • • • • • • •	\$21,000 ^{3/}	• • • • •	• • • • • • • •
Ill.	• • •	X	• • •	• • • • • • • •	\$ 9,000	X ^{4/}	• • • • • • • •
Ind.	X	• •	• • •	• • • • • • • •	• • • • • •	X ^{4/}	X
Iowa	• • •	X	• • •	• • • • • • • •	\$14,200 ^{3/}	X	X
Kans.	X	• •	• • •	• • • • • • • •	\$ 8,000	X	X ^{2/}
Ky.	X	• •	• • •	• • • • • • • •	\$ 8,000	X	X
La.	X	• •	• • •	• • • • • • • •	\$ 8,500	X	X ^{2/}
Maine	X	• •	• • •	• • • • • • • •	• • • • • •	X	X
Md.	• • •	X	• • •	• • • • • • • •	\$ 8,500	X	• • • • • • • •
Mass.	X	• •	• • •	• • • • • • • •	\$10,800	X	• • • • • • • •
Mich.	• • •	X	• • •	• • • • • • • •	\$ 9,500	X	X
Minn.	• • •	X	• • •	• • • • • • • •	\$15,300 ^{3/}	X	X ^{2/}
Miss.	• • •	X	• • •	• • • • • • • •	• • • • • •	X	• • • • • • • •
Mo.	X	• •	• • •	• • • • • • • •	\$ 8,500	X	X

(Table continued on next page)

1-7



MANPOWER[®]
TEMPORARY SERVICES

STATEMENT OF TESTIMONY
Business, Commerce and Labor Committee

RE: HB-2540, Benefit Ratio System of Employer Contribution Rates for Unemployment Taxes

DATE: February 9, 1996

FROM: Jacki Summerson, Manpower Temporary Services (913/267-4060)

My husband and I own and operate twenty-nine Manpower Temporary Services franchise offices in Kansas and Missouri. As you can imagine, in our business we have lots of payroll. Unemployment insurance is a huge expense to us every year and yet our benefit charges are fairly low. That disparity is what prompted me to investigate methods of experience rating used in other states.

First of all, let me explain that House Bill 2540 would not have any impact as long as the moratorium is in place. The change in the experience rating system would take effect when the taxes are reinstated at the end of the moratorium. This would not cause a tax increase. The Benefit-Ratio system proposed does not collect any more or less unemployment taxes than the current system. It also does not have any effect on benefits paid to workers.

UNEMPLOYMENT EXPERIENCE RATING SYSTEMS

All States have some system of experience rating by which individual employers' contribution rates are varied from the standard rate on the basis of their experience with the risk of unemployment. Kansas uses the Reserve Ratio formula to experience rate employers to determine their contribution rates.

Types of Formulas for Experience Rating. Under the general Federal requirements, the experience-rating provisions of State laws vary greatly. In each State, there are certain requirements before an employer is experience rated. For example, in Kansas, an employer must have 3 years of employment experience before they can be experience rated. The most significant variations grow out of differences in the formulas used to determine the rates. Each formula attempts to measure an individual employer's experience with unemployment. This experience then determines that employer's tax rate. At present there are four distinct systems, usually identified as Reserve-Ratio, Benefit-Ratio, Benefit-Wage-Ratio, and Payroll-Decline formulas. A

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few States have combinations of the systems. The two systems used predominately are the Benefit-Ratio system and the Reserve-Ratio system like Kansas has.

All systems have certain common characteristics. All formulas attempt to establish the relative experience of individual employers with unemployment or with benefit costs. All have factors for measuring each employer's experience with unemployment or benefit expenditures, and all compare this experience with a measure of exposure--usually payrolls--to establish the relative experience of all employers. Each formula is designed either to provide an incentive for stabilization of employment or to allocate the cost of unemployment and in turn, impacts each employer differently.

Reserve-Ratio Formula. The Reserve-Ratio was the earliest of the experience-ratio formulas. It is the formula used in Kansas and in 32 other States. Under the Reserve Ratio system, an employer's tax rate reflects his cumulative experience. All benefits ever charged against the employer are subtracted from all contributions (taxes) paid into the fund. The resulting account balance, either positive or negative, is then divided by the employer's average taxable payroll for the past 3 years. The resulting number is called the Reserve Ratio. Some states limit the number of years of contributions and benefits charged in the formula. Kansas does not. The taxable payroll used to measure the reserves is ordinarily the last 3 years but some states use as little as 1 year and others use up to 5 years. "Negative balance employers" pay a surcharge over and above their regular assigned rate.

An employer must accumulate and maintain a specified reserve before the rate is reduced. Rates are then assigned according to a schedule--the higher the reserve ratio, the lower the rate. The formula is designed to make sure that no employer will be granted a rate reduction unless *over the years* he contributes more to the fund than his workers draw in benefits.

Fluctuations in the State fund balance also affect the rate that an employer will pay for a given reserve. An increase the State fund may allow a lower rate to be assigned and conversely, a decrease in the fund balance may require higher rate.

In Kansas the formula to compute the Reserve Ratio is:

$$\frac{\text{Cumulative Contributions - Cumulative Benefits Paid}}{3 \text{ yrs. Average Taxable Wages}}$$

In general, a higher reserve ratio results in a lower contribution rate. Since this formula uses cumulative contributions and cumulative benefits paid, the experience is computed over the lifetime of the employer. A stable employer who has had few layoffs should enjoy a fairly low rate. An employer who has had regular layoffs will probably have a much higher rate and could possibly even have a negative account balance and be surcharged. If an employer had significant layoffs many years ago, but has been a stable employer for the past several years, they could still be paying a high rate even though their more recent experience has been very favorable. The formula can also cause a growing business that has a growing payroll and is creating more jobs (and therefore has few benefits paid) to receive a higher unemployment tax rate each year because their taxable wages are increasing.

This formula also allows employers who have regularly scheduled shutdowns and who have high benefits paid, to continuously remain a "negative-balance employer" and take more money out of the system each year than they will ever pay in. In essence, all "positive balance employers" are subsidizing "negative balance" employers on an ongoing basis. In any other "Insurance System", an employer like that would either have continually increasing surcharges or would be canceled. To compare, a few years ago, a surcharge was implemented in the workers compensation system to adjust for a similar situation for employers in the Assigned Risk Pool. The surcharge in workers compensation can currently go up to a maximum of 37.5% in Kansas and in some states goes up to 50%. If nothing else in our system changes, the maximum surcharge should be increased so that employers cannot continue to take more out of the system each year than they pay in.

Benefit-Ratio Formula. Under the Benefit Ratio system, contributions are not a factor. Tax rates are simply based on the ratio of an employer's benefit charges over a period to his payroll over the same period. Unlike the Reserve Ratio system, only the last few years of benefit charges are used.

The Benefit-Ratio formula also uses benefits as the measure of experience, but eliminates contributions from the formula and relates benefits directly to payrolls. The ratio of benefits to payrolls is the index for rate variation. The theory is that, if each employer pays a rate which approximates his Benefit Ratio, the program will be adequately financed.

Unlike the Reserve-Ratio, the Benefit Ratio system is geared to short-term experience. In most states, only the benefits paid in the most recent 3 years are used in the determination of the Benefit Ratios. (Some states use 4 years and some states use 5 years.) HB-2540 proposes that Kansas use 5 years.

The formula to compute the Benefit Ratio is:

$$\frac{5 \text{ yrs. Benefits Paid}}{5 \text{ yrs. Average Taxable Wages}}$$

In general, a lower Benefit Ratio results in a lower contribution rate. The end result of this formula is that unemployment taxes are tied to the actual benefits being paid out for each employer. This is more like the current system we have for experience rating worker's compensation, where an employer's experience rating is directly related to the payroll and the losses they have experienced over the past three years.

In this case, a stable employer who has hardly ever had any layoffs should enjoy a very low rate. An employer who has had regular layoffs will probably have one of the highest rates. If an employer had significant layoffs many years ago, but has been a stable employer for the past several years, they would have a lower rate computed from their past five years. A growing business that has a growing payroll and is creating more jobs (and therefore has few benefits paid) would receive a lower rate because their taxable wages are increasing and their benefits paid out are low.

Conversely, employers who are laying employees off and are paying higher benefits, would receive a higher unemployment tax rate. This method of determining employer contribution rates basically makes the employers who are taking money out of the system pay more and the employers who are not taking money out of the system pay less. More and more states are switching to the Benefit-Ratio system since it more closely reflects an employer's unemployment experience. Seventeen states currently use the Benefit Ratio system.

This system is different than the current Reserve-Ratio system in that it does not have a category for "negative-balance" employers. The way the current bill is written, it is possible that an employer who currently has a negative balance could receive a lower rate because it does not have a method to surcharge employers with high benefit ratios.

Other Formulas. Most states use one of the two formulas listed above, but a few states use a Benefit-Wage-Ratio Formula or a Payroll Variation Plan that are not as sensitive to an individual employer's experience. A chart showing the formulas used by our neighboring states is attached.

In the analysis done by the Department of Human Resources, current employers would be impacted as follows:

- 73.99% of all employers receive a ***Lower Rate Group***
- 7.56% of all employers receive the ***Same Rate Group***
- 18.45% of all employers receive a ***Higher Rate Group***

This analysis was done without taking into consideration the moratorium bill passed last year that also lowered the rates by 50%. **If the rates from the moratorium bill were included in the analysis, almost all employers would receive a lower rate.**

INDEXING THE TAXABLE WAGE BASE

HB-2540 also proposes that the taxable wage base be increased gradually by \$1,000 each year until it reaches 60% of the statewide average wage. Employers pay unemployment taxes on each employee until their wages reach the taxable wage base.

History of Taxable Wage Base. Unemployment taxes began in 1937. At that time there was no taxable wage base. The taxable wage base was implemented in 1940 at \$3,000 to comply with the federal taxable wage base. In 1940 the taxable wage base was *higher* than the state-wide average annual wage of \$1200. Today the state-wide average wage is MORE THAN \$20,000, yet the taxable wage base is \$8,000. An \$8,000 taxable wage base is less than today's minimum wage. I have attached a chart from the Department of Human Resources that shows how the taxable wage base and the average annual wage have grown apart. (See Exhibit 1.) Compare this to an income tax. If everyone paid taxes on only their first \$8,000 of income, it would be an extremely regressive tax. That is what has evolved over the years with the taxable wage base. It has made unemployment taxes regressive on employers who have low-wage, part-time or short-term workers. They are paying many times more than what their claims are. Some may say that this is fair since those workers draw unemployment more often. In fact, that is not the case. Lower paying jobs are easier to replace and those employees usually leave their short-term or

part-time job because they have found a better long term job. A comparison of the taxable wage base in other states is attached. Once again, this bill does not raise unemployment taxes, nor does it impact benefits paid.

WHO WILL PAY MORE? Many employers are drawing more out of the fund than they are paying in. In fact, of the 55,000 contributing employers in Kansas, approximately 3,000 of them have negative account balances. In other words, their employees draw more out of the fund than they pay in. The amount they are negative is significant. In 1991, those negative account employers paid in \$23 million and drew out \$49 million. In other words, they took out \$26 million more than they paid in. Negative account employers are paying in less than one-half of what their claims are. This is forcing all positive balance employers to subsidize these negative account employers. In the workers compensation reform, one of the issues addressed was that the employers in the assigned risk fund were being subsidized by all the other employers. The same situation exists in unemployment taxes. Positive balance employers are subsidizing "negative balance" employers. Increasing the taxable wage base would "level" the playing field. Since negative account employers pay the maximum amount, they would pay an increasing amount as the wage base increases. If we change to a Benefit-Ratio system, these same employers should be surcharged.

Today, the taxable wage base would increase according to the following time schedule:

1997	\$ 9,000
1998	\$10,000
1999	\$11,000
2000	\$12,000
2001	\$13,000

The wage base will stay at \$13,000 until the statewide average annual wage reaches \$23,333. Since a three year average of taxable wages is used to compute the contribution rate, the effect of the \$1,000 per year increase in the taxable wage base is even further minimized.

Changing the taxable wage base does not affect the solvency of the fund or claimant benefits. THIS IS NOT A TAX INCREASE. By statute, the State can only collect enough to maintain the fund balance. The State will not collect any more money. The contribution rates will be *reduced* accordingly so that the taxes are approximately the same.

Summary. This subject is a complex issue and is easily misunderstood. The major differences in the formulas is that the Reserve-Ratio formula is based on cumulative experience and the Reserve-Ratio formula as proposed is based on the past five years of experience. The Reserve-Ratio method is based on an Account Balance that includes contributions. The Benefit-Ratio method is more usage based system to experience rate employers. The Benefit-Ratio method is very comparable to the method used in experience rating for workers compensation. It makes the employers who are using the system pay their share.

Since we currently have a moratorium in place, any impact from changing the formula would be minimized. When the taxes are reinstated, the rates will be lower than they were regardless of

which formula is used and most employers will have a lower rate than they had before. It would be much more difficult to change it from one year to the next without the moratorium.

Unemployment Experience Rating Systems used by Neighboring States. The systems used by the states surrounding Kansas are listed below:

<u>State</u>	<u>Reserve Ratio</u>	<u>Benefit Ratio</u>	<u>Benefit Wage Ratio</u>	<u>Wage Base</u>	<u>% of State-wide Avg. Wage</u>
Arkansas	X			\$9,000	
Colorado	X			\$10,000	
Iowa		X		\$14,700	66 2/3%
Missouri	X			\$8,500	
Nebraska	X			\$7,000	
Oklahoma			X	\$10,900	50%

Comparison to Taxable Wage Base in other states. The taxable wage base in eighteen other states is currently indexed to the statewide average wage. They are listed below:

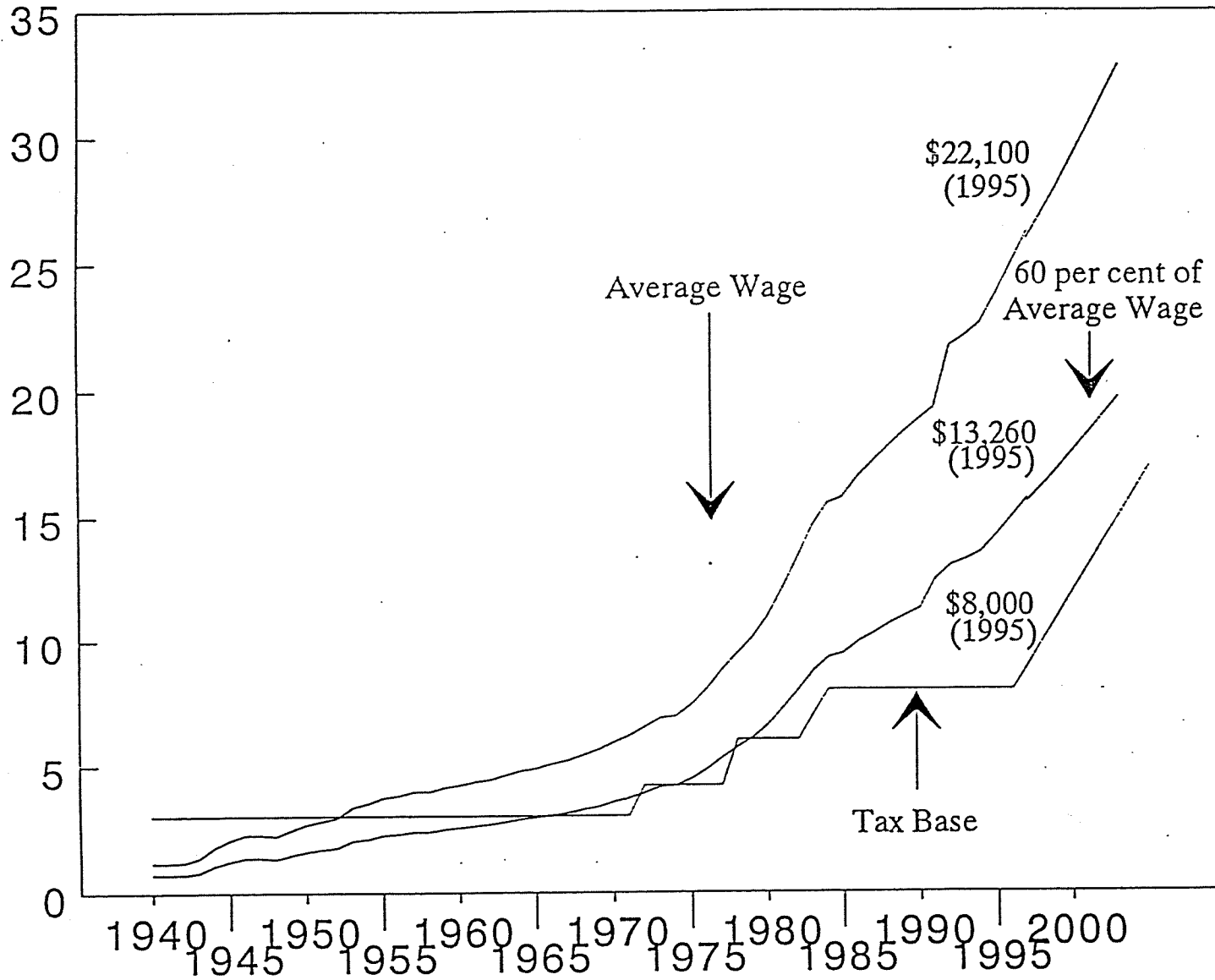
<u>State</u>	<u>Wage Base</u>	<u>% of State-wide Avg. Wage</u>	<u>State</u>	<u>Wage Base</u>	<u>% of State-wide Avg. Wage</u>
Alaska	\$24,400	75%	Hawaii	\$25,500	100%
Idaho	\$21,600	100%	Iowa	\$14,700	66 2/3%
Minnesota	\$15,800	60%	Montana	\$15,800	80%
Nevada	\$16,600	66 2/3%	New Jersey	\$18,000	54%
New Mexico	\$13,900	65%	North Carolina	\$11,600	60%
North Dakota	\$13,900	70%	Oklahoma	\$10,900	50%
Oregon	\$20,000	80%	Rhode Island	\$17,000	70%
Utah	\$17,200	75%	Virgin Islands	\$13,900	100%
Washington	\$20,300	80%	Wyoming	\$12,100	55%

States with a Taxable Wage Base above \$8,000. Most states with unemployment "experience-rating" systems similar to Kansas have already increased their taxable wage base. For example, as of January 1, 1996, the following states had a taxable wage base above \$8,000:

Alaska	\$24,400	Arkansas	\$9,000	Colorado	\$10,000
Connecticut	\$11,000	Delaware	\$8,500	District of Columbia	\$10,000
Georgia	\$8,500	Hawaii	\$25,500	Idaho	\$21,600
Illinois	\$9,000	Iowa	\$14,700	Maryland	\$8,500
Massachusetts	\$10,800	Michigan	\$9,500	Minnesota	\$15,800
Missouri	\$8,500	Montana	\$15,800	Nevada	\$16,600
New Jersey	\$18,000	New Mexico	\$13,900	North Carolina	\$11,600
North Dakota	\$13,900	Ohio	\$9,000	Oklahoma	\$10,900
Oregon	\$20,000	Rhode Island	\$17,000	Texas	\$9,000
Utah	\$17,200	Virgin Islands	\$13,900	Washington	\$20,300
Wisconsin	\$10,500	Wyoming	\$12,100		

PLEASE REMEMBER, YOU CAN'T COMPARE STATES SIMPLY BY COMPARING THEIR WAGE BASE. You must also look at their contribution rates. For example, Missouri imposed a 30% surcharge on 1996 contribution rates because their fund balance needs to be replenished.

Average Annual Wage & Taxable Wage Base
Actual 1940-1994 and Projected to 2003



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2-7