NATIONAL ASSOCIATION OF STATE WORKFORCE AGENCIES (NASWA) STATEMENT ON THE UNEMPLOYMENT INSURANCE PROVISIONS OF THE MIDDLE CLASS TAX RELIEF AND JOB CREATION ACT OF 2012

SUBMITTED BY RICHARD A. HOBBIE
EXECUTIVE DIRECTOR,
NATIONAL ASSOCIATION OF STATE WORKFORCE AGENCIES
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TO THE HOUSE COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON HUMAN RESOURCES

Mr. Chairman and Members of the Subcommittee, thank you for the opportunity to testify on implementation of the Middle Class Tax Relief and Job Creation Act of 2012 (P.L. 112-96). State Workforce Agencies are responsible for implementation of Emergency Unemployment Compensation 2008 (EUC08) and other provisions in the Act. The National Association of State Workforce Agencies (NASWA) submits this testimony for the record.

The mission of NASWA is to serve as an advocate for state workforce agencies' programs and policies, as a liaison to workforce system partners, and as a forum for the exchange of information and effective practices. Our organization was founded in 1937. Since 1973, it has been a private, non-profit corporation, financed by annual dues from member agencies and other revenue.

Our members administer critical programs including Unemployment Insurance (UI), parts of the Workforce Investment Act (WIA), Veterans' Employment and Training Services (VETS), Labor Market Information (LMI), Trade Adjustment Assistance (TAA) and employment services.

The Unemployment Insurance System in the Aftermath of the Great Recession

The UI program is an entry point to the nation's one-stop career center system for workers who lose their jobs. For many workers, this may be their first interaction with the publicly funded workforce system. State workforce agencies aim to provide income support efficiently and timely while emphasizing reemployment of UI claimants.

The UI system is a unique federal-state partnership, grounded in federal law, but administered through state law by state officials. It provides temporary, targeted, timely and partial wage replacement to laid-off workers. Created by the Social Security Act of 1935, the UI system has been a successful social insurance program for over 75 years. The system is decentralized to the state level to allow states to design and implement their own programs to mesh with their economies. State unemployment benefits are financed through state payroll taxes, which are held in individual state trust fund accounts in the federal Unemployment Trust Fund in the U.S. Treasury. The federal government finances state administration of the program with revenue collected under the Federal Unemployment Tax Act (FUTA).

Administering unemployment benefits involves four core business processes: (1) taking initial claims; (2) resolving disputes between UI claimants and employers in the claims adjudication process; (3) taking and certifying continuing claims; and (4) providing an appeals process whereby claimants or employers may appeal a state's determination of an individual's eligibility for UI benefits. States also administer employer taxes involving such processes as registering employers, handling employer wage reporting, charging benefits to individual employers and making decisions on appeals. These are complicated processes that have been made harder by insufficient federal funding for state administration and the increased workload demands stemming from the Great Recession and continuing high unemployment.

State workforce agencies have done an extraordinary job reacting and adapting to the unprecedented challenges of the Great Recession -- processing record numbers of claims and programming numerous complicated law changes. In one six-month period early in the recession -- between July 2008 and January 2009 -- weekly initial claims for UI more than tripled. In the face of continuing high unemployment, between June 2008 and the end of 2012, states implemented twelve

different federal laws extending long-term UI benefits, many of which were enacted after the program had expired. Altogether, the federal extensions provided more than $200 billion in outlays from 2008 through 2012, making the UI program the greatest contributor to additional federal spending in response to the Great Recession.

To address the unprecedented caseload volume, states made numerous staffing and other operational and business process adjustments, sometimes moving resources from lower to higher priority functions, such as from tax collection to claims processing. They also invested in new technologies to automate processes and allow for more self-service over the Internet, which a recent NASWA survey shows is continuing in the post-recession period. Despite the operational adjustments states made, state administrative performance was hurt by the Great Recession, most notably in the appeals and nonmonetary determination areas, but is moving back to normal as workloads abate.

While benefit outlays have decreased recently, we should note the rapid and unprecedented increases in workload on state workforce agencies caused by the Great Recession brought some state IT programs nearly to a breaking point. Chronic federal underfunding of the states for the administration of the UI infrastructure has left states with legacy information technology averaging 25 years old. In fact, only two states began the recession with a modernized IT benefits system. Despite recent additional funding from the U.S. Department of Labor for UI IT modernization, sufficient funding to implement major IT modernization continues to elude many states. To address this problem, NASWA proposed a UI administrative financing reform, which in effect would guarantee states would receive a total of at least 50 percent of FUTA taxes collected. If enacted, states would be better able to finance modernization of their UI IT systems.

The Middle Class Tax Relief and Job Creation Act of 2012 and the American Taxpayer Relief Act of 2012

The Middle Class Tax Relief and Job Creation Act of 2012 and the American Taxpayer Relief Act of 2012 (ATRA) extended the expiration dates of the EUC08 program and the temporary provisions of the Extended Benefit (EB) program to the end of 2013. The Middle Class Tax Relief and Job Creation Act contained complex and phased-in changes to the EUC08 program and altered the duration and state availability of each tier of the EUC08 program during three separate periods: March-May 2012, June-August 2012, and September-December 2012. States moved rapidly to implement the Act and appreciated the law kept the current tier structure intact. However, states face a significant new hurdle, which is reducing the weekly benefit amount (WBA) for EUC claimants as required under the March 1 sequestration. We address the issue of EUC sequestration at the end of this testimony.

Reemployment and Eligibility Assessments and Reemployment Services

The Middle Class Tax Relief and Job Creation Act of 2012 and the ATRA provided temporary new funding to states to provide Reemployment and Eligibility Assessments (REA) activities and Reemployment Services (RES) to EUC08 claimants. NASWA strongly supports funding to assist jobless workers return to work faster and to adopt a permanent REA/RES program, as outlined under "NASWA Recommendations." A permanent REA/RES program, modeled after the current EUC08 REA/RES program, is needed to help states reduce long-term unemployment and improve trust fund solvency.

In 2010, NASWA helped the U.S. Department of Labor (USDOL) convene a workgroup of federal, state and local partners to develop a national vision connecting UI claimants to reemployment services, drawing on state innovations and emerging technologies. If implemented nationally, the vision would ensure every claimant is viewed as a jobseeker from the point of initial filing for benefits. In combination with assessments of continuing eligibility and work search enforcement, every claimant would receive labor market information and job search assistance services.

Many UI claimants have little in-person interaction with employment and job search assistance services. Most UI claims processing occurs remotely over the Internet or telephone. Claimants usually are required to register for work, but they might not know or avail themselves of the services in local one-stop career centers, also called American Job Centers, authorized under the Workforce Investment Act of 1998 (WIA). While states and the federal government have become more interested in connecting UI claimants to reemployment services, the inflation-adjusted funding for the Wagner-Peyser Act program has been declining and has not kept pace with the growth in the labor force, nor did it respond proportionately to the near tripling of initial UI claims during the Great Recession. Moreover, most states do not have a permanent source of federal or state funding for providing REA and RES to all UI claimants exclusively.

Numerous recent evaluations demonstrate REA and RES programs reduce UI duration and are cost-effective. Reemployment and eligibility assessments and reemployment services are proven to reduce a claimant's duration on unemployment insurance benefits by two weeks or more. This may not sound significant, but a reduction of two weeks of unemployment benefits for one million workers would save about $600 million in federal benefit outlays. At a cost of say, $200 per claimant, such a program could lead to a net savings of $400 million ($600-$200 million).

The most recent research evidence[1] by Impaq International examines a program in Nevada, a state that uses the same staff to provide integrated REA and RES to UI claimants. The study found claimants in the program were much less likely than the comparison group to exhaust regular state UI. The program lowered UI duration by an average of 3.1 weeks, and reduced UI payments an average of $873 per claimant. With a cost of REA averaging $53, and RES averaging $148, for a total average cost per claimant served of $201, the program provided a $4 return on each $1 invested by government. Furthermore, the evidence shows the program "… did not just promote the early exit of claimants from the UI system; it also helped claimants obtain employment earlier than they would have in the absence of the program."

In addition to the research evidence, the implementation record to support a permanent REA and RES program is strong. Since 2008, three laws have provided temporary funding for reemployment services, including the American Recovery and Reinvestment Act (ARRA), the Middle Class Tax Relief and Job Creation Act, and the American Taxpayer Relief Act. State workforce agencies view the reemployment service programs they established under ARRA Wagner-Peyser Act funding among their greatest accomplishments. However, the Recovery Act funds, which were targeted on UI claimants receiving regular state benefits, have been spent. Many states remain highly interested in REA and RES for claimants on regular state benefits, but had to scale down or eliminate these programs.

Thanks to this Committee's leadership, two subsequent laws provided mandatory funding for REA and RES programs targeted on EUC08 claimants—those in their 27th week or more. While states have faced some challenges, which are outlined below, states were able to implement the programs on a short timeframe, and many states report they were a success from the standpoint of workers, employers and administrators.

NASWA recently surveyed states about their implementation experience with the REA and RES provisions for EUC08 claimants. The survey found the overwhelming majority of states have provided not only the mandatory services (labor market information, skills assessment, and orientations) to claimants, but also one or more of the optional services (referral to training, additional reemployment services, job search counseling, individual or group career counseling, and comprehensive and specialized assessments). Due to budget constraints, no states have reported conducting an impact analysis. However, through surveys and other NASWA forums, states have mentioned several challenges that, if addressed in future legislation, would improve the program outcomes further. The challenges are:

Temporary funding: Despite the short-term nature of the program, states had to invest in overcoming start-up challenges, with limited time to plan and execute. Start-up costs, which were not covered explicitly by the legislation, included program development, staff training, and creation of a scheduling and rescheduling process. They also experienced other management costs. The requirement for a one-on-one assessment was not something EUC08 claimants were familiar with and undoubtedly contributed to challenges such as claimants not appearing for appointments, thus requiring followup. However, now that start-up investments have been made under EUC08, even greater returns could be gained from a permanent, ongoing program.

The $85 per claimant: While states were able to implement the program at a rate of $85 per claimant, the majority of states (61 percent) reported they were not able to supplement the $85 with other funds, and funding remains a concern in many states that were able to provide only minimal services. For states that were able to rely on other workforce funding to supplement, crowding out services for other job center customers is also a concern and an unrecognized "opportunity cost." It is important to know what states have been able to accomplish with the $85 per claimant, and ensure the level of services matches what the evaluations show might be necessary to help jobseekers find work and also reduce UI duration.

[1] Michaelides, Poe-Yamagata, Benus, and Tirumalasetti, "Impact of the Reemployment and Eligibility Assessment (REA) Initiative in Nevada," January 2012, Impaq International, LLC.

<u>The "in-person" requirement:</u> According to USDOL guidance, "states must, at a minimum, require a EUC08 claimant's presence to perform the review of eligibility and review of the claimant's work search." This has proven challenging for a number of states. The guidance interprets the statutory "in person" provision to require the physical presence of each claimant at a one-stop career center or affiliate office. While the guidance permits flexibility to handle cases remotely where there would be a hardship on a claimant to appear in person, it does not recognize basic technology, such as the telephone and technologies that allow for "virtual" in-person meetings. While it is a complex task for all states, those states with the highest unemployment rates or with many rural and remote areas seem to be facing the largest challenges. In the NASWA survey, for example, a fourth of states reported facing challenges facilitating one-on-one sessions for claimants having to travel long distances.

<u>Time of engagement:</u> Early engagement of claimants in REA and RES -- targeting claimants who file their UI initial claims -- is important to producing the greatest returns for the unemployed, employers and taxpayers. Under the two recent laws, states are required to engage EUC08 claimants in REA activities within a specified period. Since EUC08 claimants in most states likely would be at least in their 27th week of UI receipt, the provisions are targeted at the long-term unemployed, not initial UI claimants. State administrators reported engaging claimants in REA and RES earlier in their receipt of UI would be more cost-effective.

<u>Work Search Requirements and Overpayments</u>

USDOL issued a guidance letter since the Act was signed into law. Unemployment Insurance Program Letter (UIPL) 5-14 (January 2013), *Work Search and Overpayment Offset Provisions Added to Permanent Federal Unemployment Compensation Law by Title II, Subtitle A of the Middle Class Tax Relief and Job Creation Act of 2012*, advising states of the mandatory requirements for work search and overpayment offsets suggests these new provisions might require amendments to state UI laws.

The Act amends UI eligibility provisions to include specific language requiring individuals to be able to work, available for work, and actively seeking work. The new law defines "as a condition of eligibility for regular compensation for any week, a claimant must be able to work, available to work, and actively seeking work." This generally mirrors what state laws already require of claimants. As USDOL's Comparison of State UI Laws finds: "In addition to registration for work at a local employment office, all states… , whether by law or practice, require that a worker be actively seeking work or making a reasonable effort to obtain work." We know of no state exceptions.

States should have the flexibility to collect the work search data in the manner that best works for them. Many states are migrating the weekly continued claim filing to their Internet process so individuals can submit a record of their work search that will be electronically linked to their UI claim. Automatically capturing the week's claim information and work search effort over the Internet should strengthen the integrity of state UI programs.

The Act also changes federal law on the collection of UI overpayments by states from "may" to "shall" collect state and federal overpayments. The new law reads:

> *A State shall deduct from unemployment benefits otherwise payable to an individual an amount equal to any overpayment made to such individual under an unemployment benefit program of the United States or of any other State, and not previously recovered. The amount so deducted shall be paid to the jurisdiction under whose program such overpayment was made. Any such deductions shall be made only in accordance with the same procedures relating to notice and opportunity for a hearing as apply to the recovery of overpayments of regular unemployment compensation paid by such State.*

States strongly support avoiding UI overpayments and collecting them when they occur. States and the federal government are making improvements in this area despite continued underfunding of federal grants to states for UI administration, the excessive workload brought about by the Great Recession, the weak recovery of employment and continuing high unemployment. Examples of improvement include the ongoing implementation of the State Information Data Exchange System (SIDES) and the use of the new federal law requiring employers to report rehires of separated employees. Both of these improvements help states make better decisions about the eligibility of UI claimants by

providing more timely information about the claimants' separations from employment and any earnings they might have while claiming UI benefits.

NASWA manages the Interstate Reciprocal Overpayment Recovery Arrangement (IRORA) agreements among states. Before USDOL issued guidance, NASWA's UI Interstate Benefits (IB) Subcommittee and UI Committee made recommendations to the NASWA Board of Directors for an updated IRORA agreement. In February 2013, the NASWA Board of Directors approved the new IRORA agreement.

The NASWA IRORA is an agreement among states to collect overpayments of unemployment benefits for each other. States can enter into separate agreements among themselves, but the IRORA provides states a standardized approach to recovering overpayments for each other on a cooperative basis. The UI IB Subcommittee is working on an electronic application for states to send requests among each other and plans to research ways states can submit electronic payments. Currently, 34 states (AK, AL, AZ, CO, FL, HI, IA, ID, IL, LA, MD, MN, MO, MS, MT, ND, NE, NH, NJ, NM, NV, OH, OK, OR, SC, SD, TN, UT, VA, VT, WA, WI, WV, and WY) have signed the 2013 IRORA agreement. Because of a USDOL directive UIPL 5-13, NASWA anticipates all states signing IRORA by the end of this year.

Short-Time Compensation

The Act included a new provision for Short-Time Compensation (STC) Program, also known as work sharing. It provides incentives for States to implement these programs and adds some new provisions with which states must comply within roughly two years. Employer participation in a state STC program is voluntary. Some new provisions require participating employers to:

- reduce hours by at least 10 percent, but not more than 60 percent;
- certify, if health and retirement benefits are provided to employees, those benefits will not be reduced due to participation; and
- submit a written plan describing how the requirements will be implemented with an estimate of the number of layoffs that would have occurred but for the program.

The STC program is not a new concept to the federal-state unemployment insurance (UI) system. Before the Act provided incentives for states, a STC program was available in selected states since the late 1970s. Twenty-two states (AZ, AR, CO, CA, CT, DC, FL, IA, KS, LA, MD, MA, MN, MO, NH, NY, OK, OR, RI, TX, VT, and WA) had introduced some type of STC program before the Act was signed into law.

The U.S. Department of Labor (USDOL) issued four guidance letters since the Act was signed into law. The guidance includes:

- Unemployment Insurance Program Letter (UIPL) 22-12 (June 2012), *Short-Time Compensation Provisions in the Middle Class Tax Relief and Job Creation Act of 2012,* provided states an overview of the new definition in federal unemployment compensation law;
- UIPL 27-12 (August 2012), *Short-Time Compensation Grant Funding*, provided states the opportunity for funding to implement or improve at state STC program as long as it conforms to Federal Unemployment Tax Act (FUTA) Section 3306(v) and is not subject to discontinuation;
- UIPL 22-12, Change 1 (December 2012), *Short-Time Compensation Provisions in the Middle Class Tax Relief and Job Creation Act of 2012,* provided states model legislation for states to use in implementing or conforming to the new definition; and
- UIPL 3-13 (December 2012), *Financing of Temporary Federal Short-Time Compensation Programs under Section 2163 of the Middle Class Tax Relief and Job Creation Act of 2012*, provided states with the opportunity to enter into an agreement with USDOL to administer a temporary federal STC program through May 2014.

Currently there are only 26 states (AZ, AR, CO, CA, CT, DC, FL, IA, KS, LA, MA, MD, ME, MI, MN, MO, NH, NJ, NY, OK, OR, PA, RI, TX, VT, and WA) offering STC programs. Eleven states (AR, CA, CT, IA, MO, NY, PA, RI, TX, VT and WA) are taking advantage of federal grants to implement or improve their STC programs.

The added workload of extending the emergency unemployment compensation program earlier this year and the recent sequestration cuts have made it hard for some states to explore this employer option. The new federal definition for the STC program has two requirements which states with existing STC programs might have to modify their UI laws in order to receive the federal funding. States will have to make sure the reduction of hours is not more than 60 percent and states must require employers to continue providing health and retirement benefits.

The Office of Personnel Management and USDOL have been communicating the availability of the STC programs to the Federal agencies in states. Federal civilian employees could be eligible to receive UI benefits under state STC programs for the unemployment compensation for federal employees (UCFE) system. An employer must submit a written plan to the state UI agency, which is subject to the state's approval. However, some state UI laws do not allow a public employer to participate in their STC programs. It should be noted that under the sequestration budget cuts federal UCFE costs could increase since federal agencies must reimburse states 100 percent of benefits costs.

Self-Employment Assistance

The Act authorizes an extension of the Self-Employment Assistance (SEA) program to include individuals who are collecting EUC consistent with the parameters of the established program. The self-employment concept was first tested in the 1990's through a series of demonstration programs and then made permanent in 1998. While the concept of offering unemployed individuals the opportunity to start a small business as an alternative to collecting benefits is in theory promising, the experience has been limited and mixed. Today only four states: Delaware, New York, Oregon, and Rhode Island, have active SEA programs.

The Act authorizes $35 million for this activity. Data from USDOL show from 1995 to 2012 the largest single year expenditure was about $17 million in 2002 and the average yearly benefits paid for the period was $10.6 million. The average number of individuals referred to an SEA program peaked at 3,170 in 2002. The average per year for the period was about 2,000 claimants. In 2012, only 1,513 individuals entered an SEA program and they received average weekly benefits of $305 for around 17 weeks.

In August 2012, NASWA partnered with Senator Ron Wyden (D-OR) and USDOL for a national webinar to promote the SEA program. Fourteen interested states (CA, CO, KS, ME, MS, MT, NJ, SC, TN, TX, VA, WA, WI, and WV) participated in the August 2012 SEA webinar discussion.

USDOL issued two guidance letters since the Act was signed into law. The guidance includes:

- UIPL 20-12 (May 2012), *The Middle Class Tax Relief and Job Creation Act of 2012 (Act) – Provisions on Self-Employment Assistance Programs,* provided information to states interested in improving an existing SEA program, developing a SEA program, or allowing EUC08/EB claimants into a SEA program; and
- UIPL 20-12, Change 1 (April 2013), *The Middle Class Tax Relief and Job Creation Act of 2012 (Act) - Extension of Application Deadline for the Self-Employment Assistance (SEA) Program Grants,* extended the deadline an additional six weeks for states to apply for Self-Employment Assistance (SEA) grants. The new deadline is now August 14, 2013.

Non-Reduction Rule

The Middle Class Tax Relief and Job Creation Act of 2012 modified the "non-reduction rule" that requires states to maintain their current weekly benefit amounts in order to receive EUC08 funding, with an effective date of March 1, 2012. Section 2144 of the Act reinstates the non-reduction rule and allows eligible states, with pending modifications of state unemployment benefits, to remain eligible for federal EUC funds through the end of the calendar year.

Before the Middle Class Tax Relief and Job Creation Act of 2012, if states failed to maintain their weekly benefit amounts, their access to EUC08 funding, 100 percent federal financing of EB and the deferral of interest and Federal Unemployment Tax Act credit reduction caps were in jeopardy.

Although Congress passed the American Taxpayer Relief Act of 2012, extending the 100 percent federal financing of the EUC08 and EB programs through December 2013, it did not address the non-reduction rule. North Carolina recently reduced the state's maximum weekly benefit amount from $535 to $350, effective July 1, 2013. USDOL has issued a termination notice to North Carolina ending the state's federal/state EUC08 agreement after June 30, 2013.

NASWA recommends the non-reduction rule be eliminated. It limits a borrowing state's options to address solvency issues by denying EUC eligibility to states that reduce weekly benefit amounts. It might have led some states to reduce potential weeks of benefits instead, thereby reducing regular state benefit weeks to the long-term unemployed. Currently, there are seven states (AR, FL, GA, IL, MI, MO, and SC) with maximum durations below what had been the system norm of 26 weeks. States should have the flexibility to determine their own regular state weekly benefit amounts and weeks of duration.

Demonstration Projects

The Act authorizes the Secretary of Labor to enter into agreements with up to 10 states that apply to conduct demonstration projects evaluating measures to reemploy UI claimants sooner than they normally would return to work. Approved demonstration projects are limited to those that: (1) subsidize employer-provided training; or (2) subsidize wages of UI claimants to pay the part of a wage that exceeds a UI claimant's weekly benefit amount. The maximum subsidy per week is the UI claimant's weekly benefit amount.

As part of the demonstration authority, the Secretary is authorized to waive the "withdrawal standard" that generally limits the use of state unemployment trust fund account funds to the payment of benefits. The applicant state must assure and provide supporting analysis that the demonstration project will not result in any net costs to the state's unemployment trust fund account during its operation. State trust funds may be used to cover the cost of the required state evaluation too, but these costs must be included in the calculation that there is no net impact on the state trust fund account. To improve the prospects of some states proposing demonstration projects, it would help states if the federal government would provide separate funds for the evaluations of these demonstration projects.

USDOL issued two guidance letters since the Act was signed into law. The guidance includes:

- UIPL 15-12 (April 2012), *Unemployment Insurance Demonstration Projects under Section 2102 of the Middle Class Tax Relief and Job Creation Act of 2012 (P.L. 112-96);* and
- UIPL 15-12, Change 1 (July 2012), *Unemployment Insurance Demonstration Projects under Section 2102 of the Middle Class Tax Relief and Job Creation Act of 2012 (P.L. 112-96*), provided additional answers to state questions.

NASWA is not aware of any state applying for a demonstration project. On July 20, 2012, NASWA, the National Governors Association, and USDOL co-hosted a webinar for the Reemployment Demonstration Waivers. Discussion centered on the UIPL 15-12 requirements. USDOL's application process covers eleven requirement areas. There also are seventeen selection factors a state has to consider when developing its proposed demonstration project. Many states expressed concern that USDOL imposed too many conditions in its application requirements. States have until October 31, 2014, to submit an application for consideration. States might need to submit their application earlier than October 2014 in order to meet the twelve-month demonstration goal. Demonstration authority expires at the end of calendar year 2015.

NASWA has one idea it would like to add to demonstration authority – reemployment bonuses. States would pay bonuses to UI claimants who return to work sooner than projected. The bonus could be graduated to pay larger bonuses for early returns to work and progressively smaller bonuses for later returns to work. Separate funding for evaluations would help in these demonstrations too.

A recent summary of the research evidence on reemployment bonuses indicates they significantly improve job search behavior and reduce the duration of unemployment. The research indicates the bonuses should be no more than three or four times a claimant's weekly benefit amount and they should be aimed at workers projected to be unemployed a long time, such as dislocated workers. Targeting workers early in their spells of unemployment who are likely to be

unemployed a long time and subsidizing their reemployment has the greatest promise for earlier reemployment and unemployment benefit savings.

Data Exchange Standardization for Improved Interoperability

The Middle Class Tax Relief and Job Creation Act of 2012 included a provision for data exchange standardization for improved interoperability. Data exchange standards are agreed upon methods for exchanging information between different systems that may store data in different formats. Interoperability in essence means the systems would be able to communicate the data. The creation of a universal data exchange standard would standardize the matching of data fields between systems. The Act also requires that the data exchange standards be nonproprietary.

Data exchange standardization could promote better service delivery, faster eligibility determinations and improved program integrity. The Act requires the Secretary of USDOL to establish these data exchange standards in conjunction with the Office of Management and Budget (OMB) and an interagency workgroup. USDOL is working on Data Exchange standards related to UI reporting.

USDOL already has supported two standardized data exchanges: the State Information Data Exchange System (SIDES) and the Interstate Connection (ICON). The SIDES facilitates exchange of information between employers and state UI programs dealing with claimant separations and also claimant benefit year earnings. The ICON facilitates the exchange of information among states for processing interstate and combined wage claims. Finally DOL is working with OMB and HHS on exploring a standardized exchange model for wage and claims reporting to the National Directory of New Hires.

Drug Testing of Applicants

The Act has two drug testing provisions: (1) it allows states to enact legislation to test UI applicants for use of controlled substances as a condition of UI receipt in claims where the UI applicant was fired because of drug use; and (2) it allows states to test UI claimants for drug use, as a condition of receipt, if suitable work for the claimant is available only in an occupation that regularly conducts drug testing. USDOL has not yet issued guidance on these provisions.

Generally, to qualify for UI, workers must have lost their jobs through no fault of their own and must be able to work, be available for work, and be actively seeking work. States disqualify workers from receipt of UI if they were discharged due to misconduct connected with work, and definitions of misconduct have developed separately in each state. As of January 2012, twenty states had specific provisions disqualifying workers from unemployment insurance if they lost their jobs because of drug use or failure to undergo drug testing, or they committed a related violation.

Spending on drug testing of UI claimants might yield savings and allay concerns about claimants' availability for work or abilities to work. However, drug tests are reported to cost $25 to $40 per test. One widely quoted study of federal government workers found 0.5 percent tested positively at an estimated cost of $77,000 per positive result. We are unaware of any evidence on drug tests of UI claimants, but states would have to weigh the costs against the potential benefits. To make informed decisions, further information would be needed.

Sequestration Reductions

The federal government imposed budget "sequestration" on March 1, 2013. Under the federal Budget Control Act, sequestration applies to many federal discretionary and some mandatory spending programs, including EUC08. The EUC08 sequestration amount represented a significant portion of non-defense reductions.

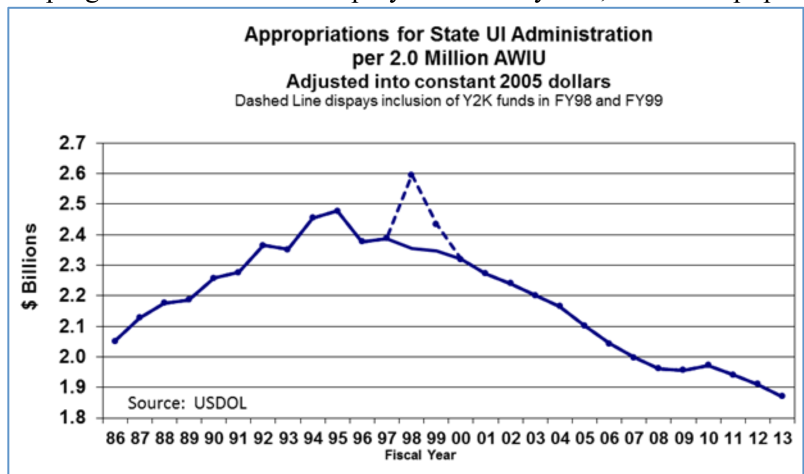
USDOL provided preliminary implementation guidance on sequestration of the EUC08 program to the states via two conference calls. On March 8, 2013, USDOL issued UIPL13-13, *Implementation of Sequestration under the Budget Control Act of 2011 for the Unemployment Insurance Programs for Fiscal Year 2013,* providing guidance on how USDOL wanted states to apply sequestration reductions to the EUC program for FY13. In USDOL's guidance, UI administration funding for regular UI, EUC08, and EB programs are reduced. States also must reduce EUC08 and EB weekly and maximum benefit amounts by selecting one of four different implementation date options: (a) March 31st at 10.7 percent; (b) April 28th at 12.8 percent; (c) June 2nd at 16.8 percent; or (d) June 30th at 22.2 percent.

What seemed to be a simple percentage change is a complex change for many states. Fifty-one states responded to a NASWA survey dated March 7, 2013, on implementing a percentage cut to the EUC08 weekly and maximum benefit amounts. A third of states said they could implement quickly, but many of the states responding said the changes could not be implemented timely or with minimal costs. In response to problems states are facing, USDOL issued UIPL 15-13, *Unemployment Insurance (UI) Supplemental Funding Opportunity to Fund Costs Attributable to the Implementation of the Sequestration Impacts on the Emergency Unemployment Compensation (EUC08) program*, for states to request additional funds for implementing the EUC08 sequestration cuts by April 12, 2013.

USDOL presently is talking to states that demonstrate they have extraordinary barriers or cannot implement the required percentage reductions. In addition, three other implementation options are being discussed by USDOL. Eleven states are exploring terminating the EUC08 agreement with USDOL as an implementation option. A few states said they will implement by June 30th, but their UI computer systems could not absorb another percentage change in October (the start of Fiscal Year 2014) and would consider terminating their EUC08 agreement then.

UI Administrative Funding

The current approach to financing UI administration does not provide adequate base funding to address the UI technology investment gap. The per-state cost of new IT benefits or tax systems ranges from $45 million to $100 million. Yet base funding, which covers the cost of administering the UI program even when unemployment is very low, has not kept pace with inflation and caseload increases for nearly two decades. Whereas base funding should reflect inflation, changes in insured unemployment, changes in productivity, and the need for ongoing capital investments, it has declined every year since the mid-1990s, and few if any states have had adequate base funding to rely on for major IT upgrades.



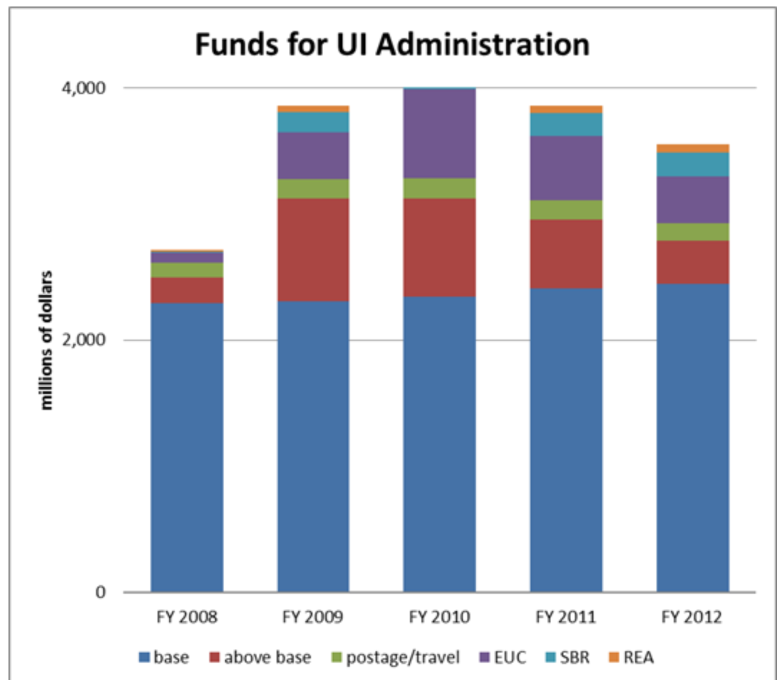
In the federal-state UI system, the federal government provides grants to states to fund the administration of state UI programs. In part, Title III of the Social Security Act says: "The Secretary of Labor shall certify…for payment to each state which has an unemployment compensation law…such amounts…necessary for the proper and efficient administration of such law during the fiscal year…The Secretary of Labor's determination shall be based on: (1) the population of the State; (2) an estimate of the number of persons covered by the State law and the cost of proper and efficient administration of such law; and (3) such other factors as the Secretary of Labor finds relevant."

The chart above shows (adjusted for inflation) federal funding for state administration of UI per two million average weekly insured unemployment (AWIU) from 1986 to 2013. Two million AWIU is a rough measure of the base workload that would need to exist to maintain operations of all state UI programs even at very low unemployment levels. The dotted line shows added federal funding to aid states making software adjustments for the year 2000 changeover. The solid line graph shows a substantial decline in real resources for base funding from about $2.5 billion in 1995 to less than $1.9 billion per two million AWIU in 2013, about $600 million less than states had been receiving. Although some of this decline might be due to productivity gains, states have long said they have not received enough base level funds to administer their programs in a proper and efficient manner even during periods of relatively low unemployment. Many states have adjusted for insufficient funds by adding state funds, roughly $180 million per year in the aggregate, but their ability to do that is dwindling as states cut their own spending to balance their budgets. And, not all states have been able to add their own state funding.

There are a number of sources of funding for state administration of UI. The main source is federal grants for administration of UI, which breaks down into base, above-base and contingency funding.

- Base funding is, in a sense, how much the USDOL determines a state needs to keep its program running regardless of how low the workload falls at or near full employment.
- Above-base funding is distributed during the year as states process workloads that exceed that funded by base funding. Conceptually, this allows USDOL to distribute funds to states that need the funds above the base funding, but after the workload has been experienced and reported by the state.
- Contingency funding is activated at the national level when the average weekly insured unemployment (AWIU) exceeds the level of AWIU that was funded in the federal budget. When a recession begins, contingency funding usually activates shortly after the beginning of the recession when unemployment increases. The formula in annual appropriations bills provides USDOL with $28.6 million per 100,000 additional AWIU above the level in the budget, which USDOL then distributes to states that have experienced the increased unemployment. This spending is designated as mandatory.

The figure below shows base, above base and contingency funding (postage/travel, EUC08, SBR and REA) for UI administration from fiscal years 2000 to 2012. Significant increases for above base (data include contingency amounts) are shown as that funding helped states cope with the recession beginning in December 2007, the last month of the first quarter of fiscal year 2008. As the graph shows, the substantial amounts in above base funding were provided in fiscal years 2009 through 2012, compared to 2008.



In addition to the regular annual funding, states can receive funds through supplemental budget requests (SBRs), which fund irregular activities, such as implementing the State Information Data Exchange System (SIDES), Reemployment and Eligibility Assessments (REA), or information technology modernization projects. States also can add their own funds to UI administration. In the aggregate, states add about $180 million of their own funds to the federal grants for administration of UI per year. However, not all states have been able to add own-state funds.

NASWA Administrative Funding Reform Proposal

NASWA urges the federal government to ensure necessary funds for proper and efficient administration of state UI programs by guaranteeing states at least 50 percent of Federal Unemployment Tax Act (FUTA) revenue collected in the previous tax year for grants to states for administration. Under this approach there would be a mixture of discretionary and mandatory spending for UI administrative funding, as there is under current law. The additional funds could be used by states to modernize their UI IT systems and for other integrity projects. NASWA provided a detailed description of this proposal to the Subcommittee in its testimony last year and would be pleased to work with the Subcommittee on the proposal.

NASWA Recommendation: A New Grant for REA and RES

States are struggling to administer their UI programs in a "proper and efficient manner" and provide REA/RES for several reasons: (1) they have said for years the federal government underfunds state grants for UI administration; (2) REA funding for state programs (not EUC) has not been provided to all states and appears to be only one-time funding provided through supplemental budget requests (SBRs); (3) RES funding has been limited, uncertain and episodic at best; and (4) inflation-adjusted funding for employment services under the Wagner Peyser Act and the Workforce Investment

Act has been cut many times, is steadily declining, and likely will continue declining as federal domestic discretionary spending is cut even more in the next few years.

In response to this struggle, NASWA suggests the federal government create a capped entitlement grant, at as much as $700 million per year, to states for REA and RES to ensure steady and sustainable funding for these important activities for the regular state UI programs. The program should be patterned after the REA/RES provisions in the Act that currently apply only to EUC claimants and should be funded out of FUTA revenue. The amount per claimant should be set higher than $85, perhaps at $200 per claimant, so some RES could be provided in addition to minimal REA services. States strongly suggest a more cost-effective approach would be to apply REA/RES to the claimants of regular state benefits early in their claims, instead of waiting until they exhaust their regular state benefits, after as much as a half year, and transition onto EUC.

NASWA is aware that creating a new entitlement grant to states for REA/RES would be challenging. However, if there is sufficient FUTA revenue coming into the federal unemployment trust fund to finance these activities and sufficient funds are not appropriated for state administration of UI and Wagner Peyser Act services, a capped entitlement would be a way for Congress to ensure states receive sufficient funds for REA/RES. This could help claimants go back to work sooner, which also could lead to lower benefit outlays and lower employer taxes in the future.

I would be pleased to answer questions any questions. Thank you.