federal register

Wednesday
August 27, 1997

Part III

Department of Labor

Employment and Training Administration

Federal-State Unemployment Compensation Program; State's Experience Rating Formula; Notice

DEPARTMENT OF LABOR

Employment and Training Administration

Federal-State Unemployment Compensation Program; State's Experience Rating Formula

AGENCY: Employment and Training Administration, Labor.

ACTION: Notice; request for comments.

SUMMARY: The Unemployment Insurance Service within the Employment and Training Administration (ETA) interprets Federal law requirements pertaining to unemployment compensation (UC) as part of its role in the administration of the Federal-State UC program.

The purpose of this notice is to obtain comments on the Department of Labor's (Department) proposal to issue more definitive direction on the Federal law requirements pertaining to the minimum acceptable interval between State UC tax rates. Although the Department's position on the need for small intervals is well established, a need for more definitive direction has been identified as a result of recent State legislative initiatives creating significant intervals between rates. This ''interval requirement'' will assure that States operate experience rating systems consistent with Federal law requirements.

DATES: The Department invites written comments on this proposal. Comments are to be submitted by October 27, 1997.

ADDRESSES: Submit written comments to Grace A. Kilbane, Director, Unemployment Insurance Service (UIS), Employment and Training Administration (ETA); U.S. Department of Labor; 200 Constitution Avenue, NW., Room C–4512; Washington, DC 20210.

FOR FURTHER INFORMATION CONTACT: Jerry Hildebrand, UIS, ETA; U.S. Department of Labor; 200 Constitution Avenue, NW., Room C–4512; Washington, DC 20210. Phone (202) 219–5200, extension 392 (this is not a toll-free number); fax (202) 219–8506.

SUPPLEMENTARY INFORMATION: The Federal and State governments are jointly responsible for administering the UC program. The legislative framework—the Federal Unemployment Tax Act (FUTA) and Title III of the Social Security Act—reserves most decisions regarding tax structure, qualifying requirements, benefit levels and eligibility/disqualification provisions to each State. However, these laws also give the Secretary of Labor responsibility for ensuring State conformity with certain Federal requirements as a condition for participating in the UC program.

One of these requirements relates to the use of experience in determining the tax rates of employers. Section 3303(a)(1), FUTA, requires, as a condition for employers in a State to receive the additional credit against the Federal tax, that State law provide that:

> no reduced rate of contributions to a pooled fund is permitted to a person (or group of persons) having individuals in his (or their) employ except on the basis of his (or their) experience with respect to unemployment or other factors bearing a direct relation to unemployment risk * * *.

Thus, Federal law permits conforming State UC laws to grant employers reduced rates only if those rates are related to the employer's experience with respect to unemployment or ''other factors bearing a direct relation to unemployment risk.'' Although the term ''experience'' is often used as convenient shorthand, no State actually measures ''experience.'' Instead what is used are ''other factors bearing a direct relation to unemployment risk.''

The words ''his * * * experience,'' as used in the FUTA, compel a State's experience rating system to measure each individual employer's experience. This means that an individual employer's rate must be assigned based on experience comparative or relative to the experience of other employers. S. Rep. No. 628, 74th Cong., 1st Sess. 50 (1935). This accomplishes the purposes of experience rating by equitably allocating costs, encouraging stabilization of employment and encouraging employer participation.

On July 31, 1940, the Social Security Board (Board), which at that time administered the UC program, published the first experience rating standards in *Employment Security Memorandum (ESM) No. 9. ESM No. 9's* explanation of the requirement that rates be assigned based on comparative or relative experience is repeated in Unemployment Insurance Program Letter (UIPL) No. 29–83, dated June 23, 1983. As stated in both issuances.

> Rate differentials are essential to any system under which an employer's rate is based on his experience, because only by the use of differentials is there a genuine reflection of the individual experience of an employer. Within the limits of the maximum and minimum rates, the smaller the intervals between the variant rates, the greater the effect of the individual experience upon the rate at which any given employer must pay contributions, i.e., the more nearly is his rate based on his experience with unemployment or other factors bearing a direct relation to unemployment risk. Numerous differentials make the transition from one contribution rate to another more equitable because if the interval between contribution rates is small, inequities to borderline employers are less than under a system in which the intervals are larger. In other words, using a large number of different contribution rates, with smaller intervals between such rates, would prevent slight variations in employer experience from resulting in large variations in rates assigned to different employers with nearly the same relative experience.

UIPL 29–83 further provides that—

> to assure that the differentiation of experience will be reflected in the rates assigned to individual employers, the rate schedule must contain rate intervals that will reasonably reflect their relative experience. A range of rates, for example, from 5.4 to 0.1, but with a highest reduced rate of 2.5 would not permit a reasonable reflection of relative experience.

In this example, the Department deems the interval between 2.5 percentage points and 5.4 percentage points (that is, 2.9 percentage points) to be inadequate to reasonably measure relative experience. Thus, if a State were to have only one reduced rate assigned to positive balance employers, and that one reduced rate was zero, the gap between that rate and the highest rate of 5.4 percentage points would be even higher (5.4 percentage points) and would simply be too large to reasonably measure relative experience.

In that situation, employers with almost identical experience would receive widely divergent rates while employers with widely divergent experience would receive the same rate. For example, in a reserve ratio State, an employer with only a $1 positive reserve balance would receive a zero percentage point rate while an employer with only a $1 negative balance would receive a 5.4 percentage points rate. Conversely, an employer with a $100,000 positive balance would receive the same zero percentage point rate as an employer of the same or larger size with a $1 reserve balance. Assigning widely divergent rates for similar experience or similar rates for widely divergent experience would both thwart the purpose of the experience rating system.

To assure experience rating continues to accomplish its purpose by reasonably reflecting relative experience, the Department proposes to establish a minimum acceptable interval between rates. Although States can and do assign rates with intervals as small as 0.1 percentage points, the Department recognizes, as stated in both *ESM No. 9* and UIPL No. 29–83, that ''administrative consideration indicate the desirability of some limitations on the number of differentials * * *.''

Given these administrative considerations, the Department proposes to establish an ''interval requirement'' of 0.9 percentage points as the *largest* percentage point interval acceptable in an experience rating system. This 0.9 percent acknowledges that some States may find it administratively desirable to have equally spaced intervals between the minimum and maximum rates. (That is, 0.0 percent, 0.9 percent, 1.8 percent and so forth up to 5.4 percent.)

Although the large interval of 0.9 percent between tax rates would less accurately reflect actual relative experience of an employer than a smaller interval such as 0.1 percentage points, the Department would not object if a State chooses to use such an interval. However, the Department would continue to encourage a State to use a system assigning a large number of rates with smaller intervals as a means of more accurately measuring employer experience and distributing the UC cost burden most fairly.

A State which does not have any interval between rates of greater than 0.9 percentage points would not need to change its law as a result of this more definitive guidance. A State with any interval between rates of larger than 0.9 percent would, however, be required to change its law. Such amendments would assure that States operate experience rating systems which more fairly allocate costs and encourage stabilization of employment by more accurately reflecting the relative experience of employers. States would be given, at a minimum, two years from the date of issuance of the Department's final position to obtain any necessary amendments to State law.

This ''interval requirement'' would apply only to ''reduced rates'' assigned by States. Section 3303(c)(8), FUTA, defines ''reduced rate'' as a rate ''lower than the standard rate applicable under state law.'' The same section defines ''standard rate'' as ''the rate on the basis of which variations therefore are computed.'' UIPL 15–86, dated February 17, 1984, provides guidance on determining the standard rate. In brief, the standard rate is 5.4 percent if the State's tax rate schedule contains a 5.4 percent rate that is assignable based on experience. If the State's law does not contain such a 5.4 percent rate, then the standard rate is the highest rate assignable based on experience under State law. To determine the effects of the proposed interval requirement on States laws, States will first need to identify the standard rate and then examine the intervals between rates at or below the standard rate.

Interested parties are invited to comment on this proposal concerning the minimum acceptable interval between tax rates.

Signed at Washington, DC on August 12, 1997.

Grace A. Kilbane,

Director, Unemployment Insurance Service.

[FR Doc. 97–22793 Filed 8–26–97; 8:45 am]

BILLING CODE 4510–30–M