Approved: March 15, 2011
Date

MINUTES OF THE SENATE COMMERCE COMMITTEE

The meeting was called to order by Chairman Susan Wagle at 8:30 a.m. on January 13, 2011, in Room 548-S of the Capitol.

All members were present.

Committee staff present:
Ms. Margaret Cianciarulo, Committee Assistant
Mr. Reed Holwegner, Kansas Legislative Research Department
Ms. Dorothy Noblit, Kansas Legislative Research Department
Mr. Ken Wilke, Kansas Office of the Revisor of Statutes

Conferees appearing before the Committee:
Ms. Kathie Sparks, Principal Analyst, Kansas Legislative Research Department

Others attending:
See attached list.

Introductions

Upon opening the meeting, Chairperson Wagle welcomed back the returning members of the Committee and Staff, introduced new people, and reviewed the Committee and conferee rules that would govern their Committee.

Introduction of bills

The Chair then called on Mr. Nick Jordan, Secretary, Department of Commerce who requested the Committee introduce two conceptual pieces of legislation,, the first is the restructuring of Kansas Inc. and second is the restructuring of KTECH. A motion was made by Senator Lynn the Committee introduce the proposed legislation. It was seconded by Senator Olson and the motion carried.

Overview of the Kansas Unemployment Fund

Next the Chair recognized Ms. Kathie Sparks, Principal Analyst, Kansas Legislative Research Department who stated she would be offering testimony of what happened when the economy experienced a massive downturn, what the projections were and what actually happened last year, and the urgent need for legislation..

She offered a brief history of the Kansas Unemployment Fund, explaining the Federal Unemployment Tax Act (FUTA), the State Unemployment Act (SUTA), negative balance employers and ineligible employers.

The Chair recognized Senator Schodorf who asked about not-for-profit organizations and government entities? (Both are also graded the same way, however they are allowed to pay-as-you-go.)

Regarding the downturn in the economy, in 2009 and 2010 Ms. Sparks stated Kansas paid out approximately $766.8M in regular program benefits and from 1-10 through 9-10, Kansas paid out approximately $429.8M. After explaining the State Extended Benefits Program and the Unemployment Insurance Trust Fund, she stated at the beginning of 2009, the Trust Fund balance was $566.6M, but by the week ending 1-2-10, the balance was $65.2M at the time, the Department of Labor (DOL) believed it would exhaust the fund sometime in February, 2010. It did, and Kansas started borrowing daily from the U.S. Treasury, but only the amount needed to satisfy benefit payments for that day. As of October, 2010, 36 states have borrowed over $40.0B in funding from the U.S. Treasury. Kansas has received $88.2M in Title X11 loans. However, as of the eighth of this month, the Kansas balance is down to $10.6M, and the next payment received will not be received until April.

The Chair asked Ms Sparks if after she has moved over to the Department of Labor, she could provide the Committee with where every state stands regarding federal advances on UI loans and how much they borrowed, so the Committee can compare them with Kansas.

Ms. Sparks went on to say, the Federal government picked up 100% of the extended benefits and forgave all interest for 2010. Also, interest on the State's loans did not start accruing until January 1,2011. She then referred the Committee to page 3, offering three charts the Department created during January of 2010 based on the estimated borrowing. They revised the charts in October, 2010.

A.) Chart 1 is what the DOL has been told what the interest payments were going to be. However, the January, 2010 projection of $42M for 2011 is wrong, because Kansas did not have to borrow what they thought they were going to.

B.) Chart 3 shows the estimate they made in October which indicates $6.2M. Chart 2 gives you a history of the U.S. Gov. interest rates. She said, this is where the legislation comes in because on September 15, 2011, the federal government will send the DOL a "bill" and this interest payment will be due in full by September 30, 2011.

She then offered three potential consequences if the interest was not paid by the required deadline including:

A.) Kansas employers may lose the offset credit against FUTA of 5.4 percent, therefore paying up to 6.2 percent against the first $7,000 of wages paid per employee,

B. Kansas may lose future borrowing privileges, and

C, Kansas would also lose all grants for costs of administration until the interest due is paid.

Federal law states you cannot use the current contributions to pay the interest payment, you have to set up a separate mechanism to pay the interest. Kansas has no such mechanism in statute. So, legislation is needed soon and any change in statute with regard to employer's rates need to occur by the first week in March so the Department will have the time needed to implement the new schedules. (To be able to send the letters out to the employers with their new calculations and these are due in April.)

The Chair recognized Senator Masterson who asked:

1.How much do we anticipate to borrow this year until our quarterly payment? (Up to $185M and in looking at the third chart on page 3, it shows only three years because what they think will happen some time next year is that we will be in the positive status again and we can use part of those funds from the regular contributions to pay down the loan.)

2. Are we building up debt and how long do we anticipate this? (The next 12 months.)

The Chair recognized Senator Lynn who stated that last year the Committee attempted to lower the amount of weekly benefits since Kansas' rates in the top three, asking is this still the case? (There were only discussions)

Regarding the principal, Ms. Sparks stated that federal law says you do not have to make a payment on the principal until you have been through two Januaries and since Kansas did not borrow until February of last year, this month is our first January, with 2012 being out second, buying us a little extra time. However, you can use the fund to pay the basic principal and they do have mechanisms. If you have not paid your loan back by November 9, of the second year, they will enact a reduction in the credit. (Remember you get the credit of 5.4% against the 6.2% and continue reducing it by .3%with the second year reduced by .6, then .9 until you have no credit. However, after the second year if they choose, they can add 2.7% surcharge on top of that to get the money back faster.) She said three states have already received their letters, Michigan, Indiana, and South Carolina. The Chair recognized Senator Olson who asked how these states are paying back their loans? (Through FUTA, they are increasing their FUTA taxes on to their employers.) Ms. Sparks also covered the 2010 enactment of **HB2676.**

In conclusion regarding the future of the Kansas Unemployment Insurance Program, she said Kansas needs a statute change for repaying the interest due September 30, 2011 and the Legislature may wish to discuss options for the repayment of the principal on the loans. Keeping in mind, one-tenth of a percent against the FUTA credit is $7.7M but they only due it in three-tenths of a percent increments (or $23M)

A copy of her testimony is (Attachment 1) attached and incorporated into the Minutes as referenced.

Minutes of the Senate Business and Labor Committee at 8::30 a.m. on January 13, 2010, in Room 548-S of the Capitol.

Adjournment

The meeting was adjourned at 9:30 a.m with the next meeting scheduled for January 19, 2011.

SENATE COMMERCE COMMITTEE GUEST LIST

DATE: 1-13-11

NAME	REPRESENTING
Caleb Reid	Sen. Pyle
Melissa Wood	Hein Law Firm
Tom Palace	PMCA of KS
Joe Mosimann	PMCA of KS
Martha Neu Smith	KMHA
Leslie Kaufman	Ks Co-ops Council
Susan Ash	Sen Hensley
Colin Curtis	Sandstone Group
Levi Henry	Coalition for Workplace Safety
Michelle Butler	Cap. Strategies
Bill Goodlatte	KRHA SHRM LDF
Natalie Bright	KS SHRM
Bruce Tunnell	AFL-CIO
Beth Krause	Sen Holland
Jeff Zehnder	WIBW-AM

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January 13, 2011

To: Senate Committee on Commerce

From: Kathie Sparks, Principal Analyst

Re: Unemployment Trust Fund

The following memorandum will explain the experience over the last two years of the Unemployment Trust Fund, including the effect of the down turn in the economy, projections estimated and actual, and the need for legislation.

History

The federal-state unemployment compensation (UC) program was created by the Social Security Act (SSA) of 1935. Unemployment compensation is an insurance program and a federal-state partnership based upon federal law, but administered by state employees under state law.

Currently, almost all wage and salary workers now are covered by the federal-state program. Railroad workers are covered by a separate federal program. Ex-service members with recent service in the Armed Forces and civilian federal employees are covered by a federal program, with the states paying benefits from federal funds and acting as agents of the federal government.

The Federal Unemployment Tax Act (FUTA) is funded by a federal tax levied on covered employers at a current rate of 6.2 percent on wages up to $7,000 a year paid to an employee. However, the law provides a credit against federal tax liability of up to 5.4 percent to employers who pay state taxes timely under a federally approved state Unemployment Compensation Program. The majority of Kansas employers do receive the maximum credit, therefore, paying a FUTA tax rate of 0.8 percent on the first $7,000 of wages or salary paid to each employee. This equates to a maximum of $56 per covered employee, per year.

The State Unemployment Tax Act (SUTA) is based on the first $8,000 of wages or salaries paid by employers for each employee. As an aside, the $8,000 amount has been in place since 1983. According to the State statutes, there are 51 positive rate classes of employers. The rate calculation is recomputed each calendar year based on the prior year's experience and total covered wages with a maximum rate of 5.4 percent applied.

When an employer's total contributions are less than the benefits paid to former employees, the employer is classified as a negative balance employer. In addition, the statutes provide for nine negative rate classes of employers who are required to pay an additional

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penalty of a maximum of 2.0 percent on top of 5.4 percent or a maximum of 7.4 percent against the first $8,000 of wages or salaries paid by employers.

A third class of employers also exist in Kansas, which are ineligible employers. Ineligible employers are new employers who do not have 24 consecutive months of payroll experience, and therefore do not have an experience rating which leads to one of the 51 positive rate classes or one of the 9 negative rate classes. Once the 24 consecutive months has been achieved, the following year, they will qualify like any other employer. Currently, all new industries or businesses, except the construction industry, are charged 4 percent. The new construction businesses are charged 6 percent because of the history of the construction industry.

Tax Years 2009 and 2010

From January 1, 2009 to December 31, 2009, Kansas paid out approximately $766.8 million in regular program benefits. In addition, the State Extended Benefits Program was triggered in 2009 when the state's seasonally adjusted total unemployment rate reached 6.5 percent or more for three consecutive months. Typically these benefits are funded partially through the state's UI Trust Fund and partially from federal funds. Through a federal Recovery Act provision, state extended benefits are funded wholly through federal funds until January, 2012. For the time period January 1, 2010 to September 30, 2010, Kansas paid out approximately $429.8 million.

As stated earlier, the Unemployment Insurance Trust Fund is funded by employers' contributions through the unemployment insurance tax and the interest earned from the money. Under state law, if the balance of the Trust Fund on July 31 of the current year meets the state's average high cost multiplier, employers can be granted a reduction in their contribution amount for the coming calendar year. Kansas' average high cost multiplier, prior to the recent recession, was 1.2, which means the balance of the Trust Fund was sufficient to provide benefits for 1.2 years at a rate equivalent to the rate during the worst three quarters of the past 20 years. These reduced contribution rates were in place during 2006, 2007, and 2008, saving employer's more than $286 million during these years.

The Trust Fund balance, as of the week ending January 9, 2010, was $65.2 million. At the beginning of 2009, the Trust Fund balance was $566.5 million. The Department of Labor, at that time, January of 2010, believed it would exhaust the fund sometime in February. This did come to pass and Kansas did start borrowing funds from the U.S. Treasury in February of 2010. Kansas and all states draw money from the Treasury on a daily basis, only the amount of money (to the nearest $1,000) needed to satisfy benefit payments for that day.

As of October 8, 2010, 36 states have borrowed over $40.0 billion in funding from the U.S. Treasury and as of the first week of January, 2011, Kansas has received $88.2 million in Title XII advances from the Federal Unemployment Account (FUA). The amount of borrowing has been far less than what was anticipated back in January 2010.

Interest Payments

The federal government normally charges interest on the loan amounts; however, for calendar year 2010, Congress waived interest for the year. The extension of the federal Unemployment Benefits does **not** waive the interest payments. In addition, the state's

Unemployment Trust Fund contributions collected cannot be used to pay interest on the advances. Interest payments must be paid from an alternative source according to federal law.

Interest began being assessed on January 1, 2011. The Department of Labor will receive a "bill" from the Treasury by September 15, 2011. Payment for the entire amount of interest will be due by September 30, 2011. **Kansas currently has no mechanism in place to make this payment.** During January of 2010 the Department made projections based on the estimated borrowing and revised these projects in October. The projections are as follows:

January 2010 Projected Interest Payments	
2011	$42,006,035
2012	$55,670,701
2013	$55,194,690
2014	$48,153,936
2015	$38,849,931
2016	$23,823,034
2017	$12,822,463

History of U.S. Gov. Interest Rate	
Year	Interest Rate (percent)
2006	4.63
2007	4.66
2008	4.81
2009	4.64
Estimate 2010	4.33

October 2010 Projected Interest Payments		
Year	Projected Interest Rate	Projected Interest Payment
2011	3.60 percent	$6.2 Million
2012	3.62 percent	$5.7 Million
2013	3.91 percent	$1.7 Million

Potential consequences of interest not paid by the required deadline are as follows:

- Kansas employers may lose offset credit against FUTA of 5.4 percent, therefore paying up to 6.2 percent against first $7,000 of wages paid per employee (currently paying 0.8 percent);

- Kansas may lose future borrowing privileges; and

- Kansas also would lose all grants for costs of administration until interest due has been paid.

Repayment of Title XII Loans

In order to assure that a state will repay any loans it secured from the Federal Unemployment Account (FUA), federal law provides that when a state has an outstanding loan balance on January 1 for two consecutive years, the full amount of the loan must be repaid before November 10 of the second year, or the federal tax on employers in the state will be increased for that year and further increased for each subsequent year that the loan has not been repaid.

Specifically, the 5.4 percent credit is reduced in successive increments of a minimum of 0.3 percent for each year in which a loan or loans remain unpaid (reducing the overall credit from 5.4 to 5.1, to 4.8 to 4.5 percent, and so forth). Additional offset credit reductions may apply to a state beginning with the third and fifth taxable years if a loan balance is still outstanding and certain criteria are not met.

As of November 10, 2010, the states of Indiana, Michigan and South Carolina had outstanding UI federal loans and as a result, employers will see an increase in their FUTA taxes. Employers in these states will see the following increase to their FUTA tax:

- Michigan: Second year in default, employers will pay FUTA of 1.4 percent (an increase of 0.6 percent);

- Indiana: First year in default, employers will pay FUTA of 1.1 percent (an increase of 0.3 percent); and

- South Carolina: First year in default, employers will pay FUTA of 1.1 percent (an increase of 0.3 percent).

Note: In Kansas, currently employers pay 0.8 percent.

Repayment of the principal on the loans can be paid from various funding sources such as reduced Federal Unemployment Tax Account (FUTA) credits; Unemployment Trust Fund (UTF) contributions, state general funds, surcharges, or additional solvency taxes.

As stated previously, the FUTA tax credit reduction begins after the second consecutive January of borrowing if the principal of the loan has not been repaid. Additional funds received as a result of the reduction are credited against the principal loan balance.

2010 Enactment of HB 2676

The Legislature enacted 2010 HB 2676 which amended the Employment Security Law regarding contribution rates, penalties, and interest. The bill provided that, for calendar years 2010 and 2011, the charge for contributing employers in rate groups 1 through 32 will be that of the 2010 original tax rate computation table which lowered the amount of funding coming into the trust fund. Contributing employers in rate groups 33 through 51 are capped at a 5.4 percent contribution rate, which is the statutory maximum rate allowed for positive balance employers. In addition, employers have 90 days past the due date to file their contribution without being charged interest for the first three quarters of each of the two years.

Conclusions

The following are the conclusions that could be reached from this memorandum about the future of the Kansas Unemployment Insurance Program:

- Kansas needs a statute change for repaying the interest due September 30, 2011. Any change in statute with regard to employers' rates need to occur by the first week of March, so the Department will have the time needed to implement the new schedules.

- The Legislature may wish to discuss options for the repayment of the principal on the loans.

If the Legislature chooses to allow the reduction in FUTA tax credits, please be advised that approximately 0.1 percent equals $7.7 million (the minimum FUTA reduction is 0.3 percent or approximately $23.0 million).

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