BEFORE THE FINANCE
COMMITTEE OF THE OHIO SENATE
SENATOR MATT DOLAN, CHAIRMAN

TESTIMONY
OF
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Mr. Chairman and members of the Senate Finance Committee, my name is Rob Brundrett and I am director of public policy services at The Ohio Manufacturers' Association (OMA). Thank you for the opportunity to provide proponent testimony on Senate Joint Resolution 4.

The OMA was created in 1910 to advocate for Ohio's manufacturers; today, it has nearly 1,300 members. Its mission is to protect and grow Ohio manufacturing.

Senate Joint Resolution 4 proposes to enact Section 18 of Article VIII of the Ohio Constitution, which would allow the General Assembly to ask Ohioans in the November 3, 2020 General Election to approve obligations to repay a loan from the federal government to the Ohio unemployment compensation fund.

Bonds are typically repaid by employer fees but a lower rate than federal loans. If SJR4 passes in November, Ohio will be able to take advantage of its provisions immediately. As noted by the resolution's sponsor, this bonding method is only to be used if the state can obtain a lower interest rate than what the federal government offers. This is not a 'silver bullet' for the serious solvency problems of Ohio's unemployment compensation system. The program itself is structurally insolvent and comprehensive reforms are needed. The OMA and allied business groups have tried for years to enact comprehensive reform legislation, which included this bonding mechanism. While the OMA supports this standalone bonding provision, more reforms will eventually be needed to ensure Ohio's program gains solvency in order to meet the next crisis.

I want to provide some context and history as to why a comprehensive solution, including this bonding proposal, is so important.

Background

The Social Security Act of 1935 (SSA) created a federal-state unemployment insurance (UI) program to (1.) provide temporary, partial wage replacement to individuals out of work, generally through no fault of their own, and (2.) promote economic stability by maintaining a steady flow of dollars throughout the economy even when there is widespread unemployment.

The UI system historically has been forward funded – i.e., a sufficient positive balance is needed in the state unemployment trust fund to avoid having to borrow to pay benefits resulting from a reasonably foreseeable economic downturn.

The UI program is a federal-state partnership conforming to federal requirements and administered by state agencies under state law. The Office of Unemployment Insurance Operations at the Ohio Department of Job and Family Services (ODJFS) administers Ohio's UI program. Administrative funds for ODJFS are allocated by the federal government from federal payroll taxes employers pay to the Internal Revenue Service.

Financing the Program

Unemployment compensation paid to unemployed workers is financed largely through both federal and state unemployment taxes paid by employers.

UI taxes are based on various factors, including the wages employers pay their employees, the type and size of the business, and the number and amount of unemployment claims filed against the business.

- At the federal level, the Federal Unemployment Tax Act (FUTA) imposes a single flat rate payroll tax on the first $7,000 of wages employers pay each employee in a year. The current FUTA tax rate is 6.0 percent. However, employers can earn credits against their FUTA tax to reflect the state employment taxes they pay. Employers who pay their State Unemployment Tax Act (SUTA) taxes in a timely manner under an approved state unemployment compensation program can earn a credit of up to 5.4 percent against the 6.0 percent, resulting in an effective tax rate of 0.6 percent.

- Each state determines its own SUTA tax rates. Some states apply various formulas to determine the taxable wage base; others use a percentage of the state's average annual wage; and a few simply follow the FUTA wage base of $7,000. Ohio's SUTA base is $9,000, with a minimum contribution rate of 0.3 percent and a maximum contribution rate of 9.4 percent.

The state assigns or computes a specific, individually determined UI tax rate for each employer annually. Every state uses some kind of "experience rating" system to determine the rate. Generally, the fewer the claims, the lower the rate the business pays in state UI taxes.

States lacking sufficient funds to pay their required unemployment benefits are authorized by Title XII of the SSA to request advances (i.e., loans) from the FUTA's federal loan fund account, the Federal Unemployment Account. If not repaid, these loans carry interest that must be paid from sources other than the state UI trust fund.

Impact of the Great Recession

The Great Recession of 2008 was the nation's longest and deepest since the Great Depression of the 1930s. A majority of states did not have sufficient balances in their state unemployment trust funds to pay benefits without requesting advances (i.e., loans) from the federal government to assure that unemployment compensation benefits were paid. Ohio was among the states hardest hit by the Great Recession. In fact, Ohio borrowed nearly $3.4 billion to cover its UI state payments.

The recession was much worse than expected, wiping out positive unemployment trust fund balances across the country and in Ohio. Automatic tax trigger provisions in Ohio law designed to address a milder recession were insufficient to meet the increased benefit payout. The size of the deficit after the recession was too great to make up with benefit cuts or tax increases alone and even years after the recession, benefit payments each year continue to be nearly as high as unemployment contribution revenue.

Failure to pay off a state's outstanding FUTA debt has costly consequences. Under federal law, if a state has an outstanding Title XII loan balance on January 1 for two consecutive years, and the full amount of the loan is not repaid by November 10 of the second year, the 5.4 percent FUTA tax credit for employers in that state will be reduced annually by 0.3 percent for each succeeding year until the loan is repaid. From the third year onward, additional reductions in the FUTA offset credit may be imposed. States that continue to have outstanding loan balances over five years in a row are subject to an even greater FUTA tax increase as a penalty for not having addressed solvency through increases in taxes and/or cuts in benefits. This also limits actions a state can make to their unemployment compensation systems.

Ohio did not repay its 2008 loan until 2017 when the General Assembly passed House Bill 390. That bill paid off the final loan amount from unclaimed funds and employers repaid the state via a one-year special assessment. At that time Ohio employers were subject to a 2.1% penalty rate on their FUTA tax as opposed to the normal 0.6% rate.

Ohio has now found itself borrowing an unprecedented amount of money from the federal government for unemployment benefits: $3.1 billion. It took Ohio nine years to pay off the previous loan. SJR4 has the potential to help alleviate some of the pain involved with an insolvent unemployment compensation system. We would urge the committee to favorably report the resolution.

I would be happy to try and answer any questions you may have.