SUBJECT: Transfer of unemployment compensation surplus credit in an acquisition

COMMITTEE: Economic and Small Business Development — committee substitute recommended

VOTE: 7 ayes — J. Davis, Vo, R. Anderson, Miles, Murphy, Reynolds, Sheets

0 nays

WITNESSES: For — (*Registered, but did not testify*: Kathy Barber, National Federation of Independent Businesses; Cathy Dewitt, Texas Association of Business; Pamela Bratton, Meador Staffing Services, Career Consultants Staffing Services; Jon Fisher, Associated Builders and Contractors of Texas; Stephanie Gibson, Texas Retailers Association)

Against — None

On — Steve Riley, Texas Workforce Commission

BACKGROUND: Labor Code, Title 4, Subtitle A is the Texas Unemployment Compensation Act. Chapter 203 establishes the unemployment compensation fund, and ch. 204 addresses employer contributions to the fund.

Sec. 204.061 sets the ceiling of the fund at 2 percent of the total taxable wages for the year ending the preceding June 30. Under sec. 204.065, if the compensation fund balance on a tax rate computation date (typically October 1) exceeds the fund ceiling, the Texas Workforce Commission (TWC) may use all or part of that surplus to provide surplus credits to employers. Under sec. 204.0651, any surplus credit TWC provides to an employer is proportional to the employer's contributions in the preceding year and is applied toward the employer's contributions due beginning with the first quarter of the following year.

Sec. 204.081 defines compensation experience as the period that benefit wage credits or benefits have been chargeable. Secs. 204.083 and 204.084 describe conditions under which TWC must, may, and may not transfer an acquired employer's compensation experience to the acquiring employer. Under sec. 204.086, an employer that acquires another employer who, at

the time of acquisition, owes TWC a contribution, penalty, or interest is liable to TWC for payment of the amount owed.

DIGEST:

CSHB 2581 would establish that an employer that acquired another employer with unused surplus credit would, under certain conditions, be entitled to that surplus credit. For an acquiring employer to be entitled to the acquired employer's surplus credit, TWC would have to have transferred some or all of the acquired employer's compensation experience to the acquiring employer. The acquired employer would forfeit any surplus credit based on compensation experience that was transferred to the acquiring employer.

If TWC determined that an employer sought the transfer of compensation experience solely or primarily to obtain a lower contribution rate, the acquiring employer would not be entitled to and could not use the surplus credit.

The bill would require TWC to adopt rules necessary to implement and enforce the section.

The bill would take effect September 1, 2011, and apply only to acquisitions occurring on or after the effective date.

SUPPORTERS SAY:

CSHB 2581 would make the unemployment insurance system fairer to employers, allowing them to inherit the benefits as well as the burdens from an acquired company. If an acquiring employer must take on a higher tax rate and pay any tax debt from an acquired business, an acquiring employer also should be able to inherit a surplus tax credit if one is due. Its current inability to do so is problematic when, for example, a sole proprietorship incorporates and cannot carry its surplus credits forward. Hundreds of employers have been unable to receive the surplus credit of an acquired business, and many have filed appeals with TWC. CSHB 2581 would save both employers and TWC the time and money associated with these appeals by clarifying the law.

CSHB 2581 would allow TWC to develop the surplus credit transfer process so that it would ensure employers could not game the system and were not simply buying another company to acquire its surplus credit.

Although the surplus credits that would be transferred under the bill currently are retained in the unemployment compensation fund, the

Legislative Budget Board reports that the bill would not have a significant fiscal impact on the state and would not create or impact any state tax or fee. TWC recommended the bill's changes, and numerous prominent business trade associations support the bill.

OPPONENTS SAY:

CSHB 2581 could weaken the already fragile unemployment compensation fund. The ceiling of the fund is so low that it cannot build up enough reserves in good economic times to provide unemployment insurance benefits to all who qualify for them in bad economic times. The last time the fund balance exceeded the ceiling, in 2007 and 2008, TWC gave out nearly $450 million in surplus credits, which are essentially tax rebates, and the fund was drained to the point of no longer covering liabilities. Less than two years later, when the economy soured, the fund balance dropped beneath the statutory floor, and the state was forced to borrow more than $1 billion from the federal government, issue $2 to $3 billion in bonds, and nearly triple the minimum employer unemployment tax rate to cover benefits.

Given the extreme volatility of the unemployment compensation fund, the state should be safeguarding as much of the fund as possible, rather than considering new ways of rebating it to a small subset of employers, as CSHB 2581 would do. In the long run, minimizing rebates would benefit every Texas employer by avoiding the massive tax hikes that currently accompany economic downturns.

OTHER OPPONENTS SAY:

The primary goal of CSHB 2581, to establish equity between acquiring a purchased employer's debts and acquiring its credits, is reasonable and fair. However, due to the volatility of the unemployment compensation fund and the exacerbating effects of surplus credits when the fund balance rises above the ceiling, additional surplus credits should be authorized only in conjunction with raising the ceiling of the fund. Pairing these changes would make the unemployment system both fairer and more stable for Texas employers.

NOTES:

The committee substitute differs from the bill as filed in that it would entitle a qualifying acquiring employer only to an acquired employer's surplus credit and not also to its surplus credit rate. The substitute deleted a provision that would have specified that, if an acquiring employer acquired only a part of an employer and received only the corresponding part of its compensation experience, the acquiring employer would be

entitled only to the corresponding part of the acquired employer's surplus credit.

The companion bill, SB 638 by Jackson, passed the Senate by 31-0 on the Local and Uncontested Calendar on March 24 and was reported favorably, without amendment, by the House Economic and Small Business Development on April 12, making it eligible to be considered in lieu of HB 2581.