Benefits and Risks of Reimbursing for Unemployment

Benefits to Reimbursing for Unemployment

For many employers, the benefits of becoming a reimbursing employer far outweigh the risks of assuming all responsibility for unemployment claims. Some key benefits include:

- Cost Savings
- Better Financial Control

Cost Saving Benefit

There are three main areas where employers can realize a cost savings by becoming a reimbursing employer:

- Overpaying/Subsidizing State Pool
- Lag State Benefits
- Fluctuating State Unemployment Taxes

A. Overpaying/Subsidizing State Pool

Based on a recent analysis done of 501(c)(3) nonprofits, it was found that nearly 86% of those paying SUI taxes are overpaying. Meaning they pay more money in taxes/benefits than they ever cost the state in unemployment claims. They are therefore funding benefits of other employers in their state including for-profit employers. Employers who pay only for their own unemployment charges save money by not paying into a government pool that pays claims for everyone else's unemployed employees.

B. Lag State Benefits

Thirty-three states are defined as "lag states" (find a list of those states here) which means during the first year after an employer becomes a reimbursing employer any claims paid out from January to (approximately) September are paid out of the employer's original state unemployment benefits account, and not charged to the employer for reimbursement. Strategic management of this initial benefit can result in substantial one-year savings.

C. *Fluctuating State Unemployment Taxes*

Each state determines how their unemployment insurance benefits pool is funded. Two factors are used to calculate an employer's contributions:

- State Taxable Wage Base
- Tax Rate Schedules

The wage bases and tax schedules are leveraged a different way in every state. Some states manage their unemployment better than others. Some states amassed huge debts during the last recession and their tax rates have remained relatively high to pay off those debts.

A few states did not enjoy the way their unemployment systems performed during that recession, so they are implementing them in new ways. This can mean unannounced changes to taxes, claims payments and taxable wage bases.

In other states, the taxable wage base is indexed to the average wage or some other method. In those states the employer will most likely see their costs continue to rise even if their tax rate decreases somewhat. Also, tax rates are based on experience. If an organization has a recent history of no-fault layoffs, their unemployment taxes will increase to match their poor claims history – regardless of state-wide unemployment.

Better Financial Control

Reimbursing employers have removed their organizations from the state managed unemployment insurance program so that they can manager their own individual programs. This allows them, through tools like third party administrators and custom insurance policies, to more actively control their annual unemployment insurance liability. They are less vulnerable to evolving state economic conditions and the actions of state legislatures. The can almost to the penny know how much their unemployment insurance is going to cost them from year to year. This allows for better utilization of their entire budget.

Risks of Reimbursing for Unemployment

Opting out of the state unemployment program has many rewards, but also a few risks. The key risk that the employer is moving out of a fully insured program to assuming all the costs of unemployment benefits paid out to separated employees. Qualifying employers with high or unpredictable employee turnover are not good candidates for reimbursing as the unforeseen expenses may strain budgets and be difficult to predict. Reimbursing employers should maintain proper funding reserves to pay for unemployment claims. Proper reserves protect the employer from unexpected layoffs or a catastrophic loss of funding.

Another risk – for any employer – in either the merit/tax program or as a reimbursing employer, are erroneously claims paid out by the state and charged to employers. Every year, the Department of Labor must publish a list of those improperly paid payments. The latest published report (2017) showed a nationwide total of 3.8 billion! Closely monitoring every claim is a wise exercise for every employer.