
Testimony on Senate Bill 81

Policy Matters Ohio
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Mr. Chairman, honorable members of the committee, thank you for this opportunity to present testimony on Senate Bill 81. We support the timely movement of this legislation and your efforts to comply with federal mandates. Our testimony draws on the work of the National Employment Law Project, a national advocacy group working on behalf of low-wage workers and the unemployed.

Our comments address one element of this bill: Clauses that address State Unemployment Tax Act dumping, commonly called SUTA dumping. SUTA dumping, the practice of shifting payroll responsibility to entities bearing a lower level of unemployment taxation, costs state unemployment funds around the country many millions of dollars annually.

For example, the state of Michigan recently recovered \$2.4 million in its first anti-SUTA dumping action against the Aramark Corporation. Other states' experience is similar. Connecticut has discovered a loss of \$4 million since October 2003, and has dozens of cases pending. North Carolina collected \$9 million in just 12 cases, with 250 cases still pending.

Kelly Services, a major proponent of SUTA dumping legislation, estimates it could have saved \$30 million in taxes in one year if it had engaged in SUTA dumping.

While the exact scope of the problem in Ohio has not been precisely measured, there is little reason to think it is any different here. At a meeting last spring of the legislative subcommittee of the Unemployment Compensation Advisory Council, ODJFS Assistant Deputy Director William Lind cited one large employer in Ohio that had a couple of thousand employees, and was paying at the 3.8 percent rate. It bought a floral business that had reported a 0.2 percent rate, and switched to the lower rate, to the detriment of the fund. So clearly, Ohio is not immune to this problem.

Conforming to federal requirements of the SUTA dumping prevention legislation of 2004 is mandated; however, it is possible for states to safeguard their funds over and above the minimum safeguards used in Senate Bill 81. In particular, there are two places in this bill where we recommend a higher level of safeguards:

1) We recommend that SUTA dumping prevention be extended to Professional Employee Organizations.

The business of using a professional employee organization (PEO) in order to save money on payroll taxes is large and growing. PEOs provide “payrolling” services, allowing a company to move part of, or its entire, regular workforce on to the official payroll of the PEO which handles all benefits and taxes. PEOs are different from payroll services, because the workforce becomes official employees of the PEO.

Senate Bill 81 does not cover the practice of firms leasing their employees to a professional employee organization in order to rid themselves of their unemployment insurance tax experience. Under this arrangement, employees are “dumped” from an existing business to a PEO, but since the two businesses are not under “common ownership or control,” the PEO would not be forced to combine its experience with the new firm. Thus, the main firm is able to rid itself of its unemployment tax experience.

As other SUTA dumping schemes are cut off, PEOs may become a more attractive option to firms looking to artificially lower their unemployment tax expenses.

For your consideration in thinking about how this issue might be addressed in Ohio, we provide a clause from legislation under consideration in Minnesota:

*“Any person that contracts with a taxpaying employer to have that person obtain the taxpaying employer's workforce and provide workers to the taxpaying employer for a fee shall, as of the effective date of the contract, be assigned for the duration of the contract the taxpaying employer's account. That tax account must be maintained by the person separate and distinct from every other tax account held by the person and identified in a manner prescribed by the commissioner. The tax account shall, for the duration of the contract, be considered that person's account for all purposes of this chapter. The workers obtained from the taxpaying employer and any other workers provided by that person to the taxpaying employer must be reported on the wage detail report under that tax account, and that person shall pay any taxes due at the tax rate computed for that account.” (proposed legislation in **Minnesota H.B. 898**)*

2) We recommend stiffer penalties on tax advisors.

SUTA dumping is a tax avoidance scheme invented by tax advisors, among them some of the biggest accounting firms in the country. Senate Bill 81 imposes certain penalties on “persons” who “knowingly” violate or attempt to violate the law. However, its strongest penalty, for “employers” who violate the law, will likely not cover many tax advisors.

Even if the penalties do apply to most tax advisors, they will apply only with respect to the tax advisor’s own payroll, rather than to the payroll of the SUTA-dumping company.

Most tax advisors will probably be penalized as “non-employers” under the law. This means that the only penalty that attaches to a tax advisor is a maximum \$5,000. This amount is clearly not sufficient to deter tax advisors from encouraging companies to dump their payroll taxes, given the amounts of money at stake.

We want to reinforce our concern that this is not a minor problem. State statistics provided to the Government Accountability Office in 2002 show that the average amount of taxes underpaid by SUTA dumping businesses was more than \$600,000.

The new California law provides for penalties of \$5,000 or 10% of the taxes unlawfully underpaid specifically on tax advisors, whichever is higher. More stringent penalties also have been proposed in other states. We suggest that you consider the following provision, which has been proposed in a bill in Arizona:

“If a person knowingly attempts to make or makes a transfer of business for the purpose of obtaining a lower rate of contribution or if another person aids such a person in evading or defeating a contribution or its payment, the Department shall assess against the person a civil penalty of five thousand dollars or fifty per cent of the amount of any taxes that are underpaid, whichever is greater.” (Arizona H.B. 2616)

Thank you for your consideration of our comments, and I would be glad to answer questions.