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Federal bill targets unemployment fraud

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Expected to close loopholes in tax payments

President Bush is expected to sign a bill that would force states to bar employers from shirking their unemployment insurance tax obligations by shifting their payrolls from one company to another.

Maryland already has an insurance fraud prevention law, but the federal reform is already sparking discussion about whether the state measure is tough enough.

Tax rates for unemployment insurance depend on how often workers from a company file for jobless benefits. The more layoffs and firings, the higher the rating. Because new companies automatically start out with a low rating, some employers escape paying high rates by creating a new company and "dumping" most or all of their employees into it.

How much money disappears through this loophole remains unknown. In many states, it is not even illegal. But according to the Government Accountability Office, formerly called the General Accounting Office, hundreds of millions of tax dollars -- money often replaced by increasing premiums for other employers -- are believed to be lost each year as a result.

The bipartisan reform measure, passed by the House on July 14 and the Senate on July 23, would require states to enact laws that would close the loophole and impose penalties on employers caught perpetrating the fraud.

"It's very difficult to enforce under the state law without the federal government providing the overall guidelines," said U.S. Rep. Benjamin L. Cardin (D-Dist. 3) of Baltimore, ranking Democrat on the House Human Resources Subcommittee and a co-sponsor of the bill. "And these companies are not just Maryland companies, so it's not easy for a state to do it alone."

It is already illegal under Maryland law for employers to willfully misrepresent and manipulate their payroll to dodge unemployment insurance tax liability.

The state cross-matches companies that close down with the appearance of new companies of similar size in the same sector to make sure employers are not shifting employees around to avoid taxes, said Susan R. Bass, unemployment insurance policy and planning supervisor at the state Department of Labor, Licensing and Regulation.

The department has no evidence suggesting that the practice is a serious problem, she said.

But dumping employees does not necessarily require a company to shut down altogether and may even take the form of "leasing" employees between companies, said Paul Desaulniers, special agent for the GAO's investigative branch.

Evading unemployment insurance taxes in Maryland is a misdemeanor, not a felony, with a penalty of only a $1,000 fine and up to 90 days in jail.

At a risk of only $1,000, Desaulniers asked, "if you could save $2 million, would you?"

Cardin said he is not convinced that tax evasion does not occur in Maryland and believes the state needs to re-examine its law now that the federal measure is about to be enacted.

"Maryland does have a problem; this is a nationwide problem," he said. "I think they don't know the extent of the issue because they don't have complete records of it."

The federal measure does not specify the penalties the state laws should carry, other than stipulating that "meaningful civil and criminal penalties" must be imposed on violators.

Maryland law may need some reform, said Deborah Povich, executive director of the Job Opportunities Task Force in Baltimore and a member of the state legislature's Unemployment Insurance Task Force.

"I think we'd be very interested in strengthening the penalties, and changing the law as needed to make it as effective as possible," Povich said. "The truth is, strengthening the penalty for SUTA [State Unemployment Tax Act] dumping would probably be the easiest thing the task force could do ... it would be a welcome part of the solution."

Another provision of the federal reform bill also would help states combat insurance fraud on the benefits side. The bill grants insurance administrators access to a National Directory of New Hires, allowing them to cross-reference that list against their state's list of unemployment benefits recipients.

Maryland already cross-references a record of new hires in the state with its list of unemployment benefits recipients to ensure no one is collecting benefits in Maryland while working here.

In the first six months of the year, the cross-checking of in-state lists yielded $1,225,270 from 3,591 cases where no fraud was charged and $726,313 from 926 cases where fraud was identified.

"But we have had no access to new hires collecting wages out of state," Bass said. "This will help in recovering improperly paid unemployment benefits ... this may be an area where we may not know that there has been a problem."