

Preliminary Performance Review

**Unemployment Compensation
Division**

**The Legislature Should Consider Establishing
An Enforcement Mechanism That Allows
Business Registration Certificates To Be
Revoked At Any Time Between Renewal
Periods For Employers Who Are
Delinquent In Paying Unemployment Taxes**



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John Sylvia
Director

October 2, 2005

The Honorable Edwin J. Bowman
State Senate
129 West Circle Drive
Weirton, West Virginia 26062

The Honorable J.D. Beane
House of Delegates
Building 1, Room E-213
1900 Kanawha Boulevard, East
Charleston, West Virginia 25305-0470

Dear Chairs:

Pursuant to the West Virginia Sunset Law, we are transmitting a Preliminary Performance Review on the *Unemployment Compensation Division*, which will be presented to the Joint Committee on Government Operations on Sunday, October 7, 2005. The issue covered herein is "The Legislature Should Consider Establishing An Enforcement Mechanism That Allows Business Registration Certificates To Be Revoked At Any Time Between Renewal Periods For Employers Who Are Delinquent In Paying Unemployment Taxes."

We transmitted a draft copy of the report to the Unemployment Compensation Division on September 16, 2005. The Division opted not to have an exit conference. We received the agency response on September 23, 2005.

Let me know if you have any questions.

Sincerely,

Handwritten signature of John Sylvia in cursive script.
John Sylvia

JS/wsc

Joint Committee on Government and Finance

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Executive Summary

Issue 1: The Legislature Should Consider Establishing An Enforcement Mechanism That Allows Business Registration Certificates To Be Revoked At Any Time Between Renewal Periods For Employers Who Are Delinquent In Paying Unemployment Taxes.

The Unemployment Compensation Division has a long history of collecting over 99% of the unemployment tax each year.

Defaulted employers can operate and accumulate debt for up to two years.

The Unemployment Compensation Division has a long history of collecting over 99% of the unemployment tax each year. The Legislative Auditor commends the Unemployment Compensation Division for its enforcement efforts. However, since the Legislature required the Department of Revenue to begin issuing business registration certificates with a biennial renewal period, defaulted employers can operate and accumulate debt for up to two years. Authorizing the additional enforcement mechanism of revocation between renewal periods would be beneficial to the Division. The importance of such authority was recently recognized by the Legislature with the passage of Senate Bill 2013 during the 2003 Second Special Session, which authorized the Department of Revenue to revoke the business license of employers who defaulted on their workers' compensation premiums. **Therefore, the Legislative Auditor recommends that the Legislature give the Division and the Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes.**

Recommendation

1. *The Legislative Auditor recommends that the Legislature give the Division and the Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes.*

Review Objective, Scope and Methodology

This Preliminary Performance Review of the Unemployment Compensation Division is required and authorized by the West Virginia Sunset Law, Chapter 4, Article 10 of the West Virginia Code.

Objective

The objective of this report was to determine the extent to which employers were operating without paying unemployment taxes.

Scope

This report used information on defaulted employers as of July 2005. Some historical data were provided for informational purposes.

Methodology

The Unemployment Compensation Division provided the Legislative Auditor with a list of all active, defaulted employers as of July 2005. The Legislative Auditor then sorted the list by employers who were bankrupt, under a repayment agreement, had not had their license come up for renewal, or did not have a valid business license. The Legislative Auditor also received the benefits paid to the employees of defaulted employers since the employers first became delinquent. Every aspect of this evaluation complied with Generally Accepted Government Auditing Standards (GAGAS).

Issue 1

The Legislature Should Consider Establishing An Enforcement Mechanism That Allows Business Registration Certificates To Be Revoked At Any Time Between Renewal Periods For Employers Who Are Delinquent In Paying Unemployment Taxes.

Issue Summary

The Legislative Auditor found that there are only approximately one-percent (1%) of employers who are on the Division's default list. The amount that these employers owe is about \$3.4 million, as of July 2005.

The Unemployment Compensation Division has a long history of collecting over 99% of the unemployment tax each year. Its enforcement efforts were strengthened in 1996, when the Legislature amended the Unemployment Compensation Code to allow the Division to file criminal charges against a defaulted employer. In that same year, the Department of Revenue was authorized to deny issuing a business license to any employer who was not in good standing with the Division. These stronger enforcement tools have contributed to a high collection rate. The Legislative Auditor found that there are only approximately one-percent (1%) of employers who are on the Division's default list. These are employers who are conducting business while owing two or more quarters of unemployment taxes. The amount that these employers owe is about \$3.4 million, as of July 2005.

The Legislative Auditor commends the Unemployment Compensation Division for its enforcement efforts. Despite the Division's high collection rate, there is another enforcement tool that the Division should have to enhance its enforcement efforts. It should be noted that in 1999, the Legislature required that all business registration certificates be issued for a two-year period instead of one year. The effect of this change is that it will be two years before the Department of Revenue can deny renewing a business registration to a business in default in the unemployment tax. This allows employers two full years of operation despite being in arrears. The threat of a business registration certificate not being renewed is a strong incentive for a defaulted business to become current in the unemployment tax. The extra year delays the time in which the delinquent tax is paid to the Division and it increases the amount owed. This could cause the amount of unemployment taxes that are eventually written off to be higher because a business has an extra year before its business registration certificate comes due. The Division indicated to the Legislative Auditor that it is not uncommon for some employers to pay the delinquent unemployment tax at the time of renewing their business registration certificates and then soon after become delinquent for the next two years. **The Legislative Auditor recommends that the Legislature give the Division and the**

Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes. This authority has been recently granted to the Department of Revenue and the Workers' Compensation Commission.

The Unemployment Compensation Division Has A High Collection Rate

Since 1987, the Unemployment Compensation Division has collected an average of 99% of all unemployment taxes due.

Since 1987, the Unemployment Compensation Division has collected an average of 99% of all unemployment taxes due. The Legislative Auditor commends it for this collection rate. In 1996, the Division had its enforcement powers strengthened by an amendment to the Code. That amendment provided two additional enforcement mechanisms: 1) the authority to file criminal charges against defaulted employers; and 2) the authority for the Department of Revenue to deny the renewal of a business registration certificate. Both enforcement tools have facilitated the high collection rate. Table 1 shows the average quarterly collection rate of the Unemployment Compensation Division since fiscal year 2000. Although there appears to be a decline in the last two years, this reflects the lag time in future collection efforts before the collection rate reaches 99%.

Fiscal Year	Average Quarterly Collection Rate
2000	99.92%
2001	99.80%
2002	99.77%
2003	99.30%
2004	98.49%
2005 ¹	97.64%

*Source: Data for this table were provided by the Unemployment Compensation Division.
¹ Data for Fiscal Year 2005 are only for the first two quarters.*

Defaulted Employers May Operate for Up to Two Years

Despite the high collection rate, the Unemployment Compensation Division could benefit from one additional enforcement mechanism. Under West Virginia Code, the Department of Revenue will deny the renewal of a business registration certificate if employers have defaulted on their unemployment taxes. The Department, however, may not revoke a license prior to the renewal date with respect to employers who are delinquent on unemployment taxes. It should be noted that in 1998, the Legislature required that all business registration certificates have a two-year renewal cycle beginning July 1, 1999. Given that there is no provision allowing for the revocation of a business registration certificate, this had the unintended effect of increasing the length of time a defaulted employer could operate before facing the loss of a business license. In addition, the Division indicated to the Legislative Auditor that it is not uncommon for some employers to pay the delinquent unemployment tax at the time of renewing their business registration certificates and then soon after become delinquent for the next two years.

The majority of defaulted employers operate because their license has not come up for renewal.

As a result, the majority of defaulted employers operate because their license has not come up for renewal. These employers will continue to accumulate debt and interest until the two-year cycle lapses. During this time, the employers could accumulate too much debt to pay, and go out of business or choose to operate illegally. **Therefore, the Legislative Auditor recommends that the Legislature give the Division and the Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes.** The Legislature has previously recognized the value of such authority with the passage of Senate Bill 2013 in the 2003 Second Special Session. The passage of Senate Bill 2013, which established the Workers' Compensation Commission, also authorized the Department of Revenue to revoke a business license if an employer was in default with the Commission.

Table 2			
Defaulted¹ Employer Breakdown			
Reason for Operation	Number Operating	Percentage of Defaulted Employers	Amount Owed
Repayment agreements.	110	21%	\$869,000
Inability to revoke the business license prior to the renewal date.	367	69%	\$530,000
Bankruptcy protection.	21	4%	\$580,000
Operating illegally ² .	37	7%	\$1,300,000
Total	535	100%	\$3,279,000

Source: Data for this table were provided by the Unemployment Compensation Division and the Department of Revenue.

¹*West Virginia Code defines a defaulted employer as any employer owing two or more quarters, which need not be consecutive but within 25 quarters of each other, of unpaid unemployment taxes, penalties, and interest.*

²*This group also includes eight employers who have been enjoined from doing business, yet are continuing to operate.*

There are 34 defaulted employers in business who are operating without a business license.

As of July 2005, employees of active, defaulted employers had been awarded over \$2.3 million in benefits since the employers became defaulted.

The Unemployment Compensation Division has maintained a high collection rate since 1987, and the Legislative Auditor commends it for this effort.

However, even with increased authority, some employers will still not pay. There are 34 defaulted employers in business who are operating without a business license. They collectively owe approximately \$1.3 million in unemployment taxes. Despite the default status of these employers, the Division must continue to pay out benefits to their employees. **As of July 2005, employees of active, defaulted employers had been awarded over \$2.3 million in benefits since the employers became defaulted.** The benefits paid out to employees of the delinquent employers came from taxes paid by other businesses in good standing. This places a burden on employers who remain current, and may serve to further deplete the trust fund.

Conclusion

The Unemployment Compensation Division has maintained a high collection rate since 1987, and the Legislative Auditor commends it for this effort. Although defaulted employers account for only 1% of all employers paying unemployment taxes, the majority of defaulted employers are businesses with a valid business license. However, since the Legislature required the Department of Revenue to begin issuing business registration certificates with a biennial renewal period, defaulted employers may operate and accumulate debt for up to two years. Allowing the additional enforcement mechanism of revocation between renewal periods would be beneficial to the Division. The importance

of such authority was recently recognized by the Legislature with the passage of Senate Bill 2013 during the 2003 Second Special Session, when authorized the Department of Revenue to revoke the business license of any employer that defaulted on their workers' compensation premiums. **Therefore, the Legislative Auditor recommends that the Legislature give the Division and the Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes.**

Recommendation

1. *The Legislative Auditor recommends that the Legislature give the Division and the Department of Revenue the authority to revoke a business registration certificate at any time between renewal periods in order to minimize the loss of unemployment taxes.*

Appendix A: Transmittal Letter

WEST VIRGINIA LEGISLATURE *Performance Evaluation and Research Division*

Building 1, Room W-314
1900 Kanawha Boulevard, East
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John Sylvia
Director

September 16, 2005

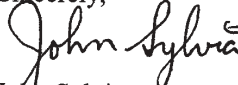
Daniel Light, Director
Unemployment Compensation Division
112 California Avenue
Charleston, West Virginia 25305-0112

Dear Director Light:

This is to transmit a draft copy of the Preliminary Performance Review of the Unemployment Compensation Division. This report is scheduled to be presented during the October 2nd- 4th interim meeting of the Joint Committee on Government Operations. We will inform you of the exact time and location once the information becomes available. It is expected that a representative from your agency be present at the meeting to orally respond to the report and answer any questions the committee may have.

If you would like to schedule an exit conference to discuss any concerns you may have with the report, please notify us. We need your written response by noon on Friday, September 23, 2005 in order for it to be included in the final report. If your agency intends to distribute additional material to committee members at the meeting, please contact the House Government Organization staff at 340-3192 by Thursday, September 29, 2005 to make arrangements.

We request that your personnel not disclose the report to anyone not affiliated with your agency. Thank you for your cooperation.

Sincerely,

John Sylvia

Joint Committee on Government and Finance

Appendix B: Agency Response



Joe Manchin III
Governor

Ronald E. Radcliff
Director

September 21, 2005

RECEIVED
SEP 23 2005

PERFORMANCE EVALUATION AND
RESEARCH DIVISION

John Sylvia
Director
West Virginia Legislature
Performance Evaluation and Research Division
Building 1, Room W-314
1900 Kanawha Boulevard, East
Charleston, WV 25305-0610

RE: Your letter dated September 16, 2005

Dear Mr. Sylvia:

I have reviewed the draft copy of the Preliminary Performance Review of the Unemployment Compensation Division and have no concerns to express at this time. Therefore, I see no need to schedule an exit conference.

Agency representatives will be available to appear before the Joint Committee on Government Operations during the October 2nd-4th interim session. We do not intend to distribute additional material to committee members at the meeting.

We certainly will honor your request that information in this report will not be disclosed to anyone not affiliated with our agency before it is released by you.

Thanks for sharing the information.

Sincerely,


Daniel Light
Director

DLL/emk

pc: Ronald Radcliff
Donald Pardue
Brian Armentrout
Noah Browning

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