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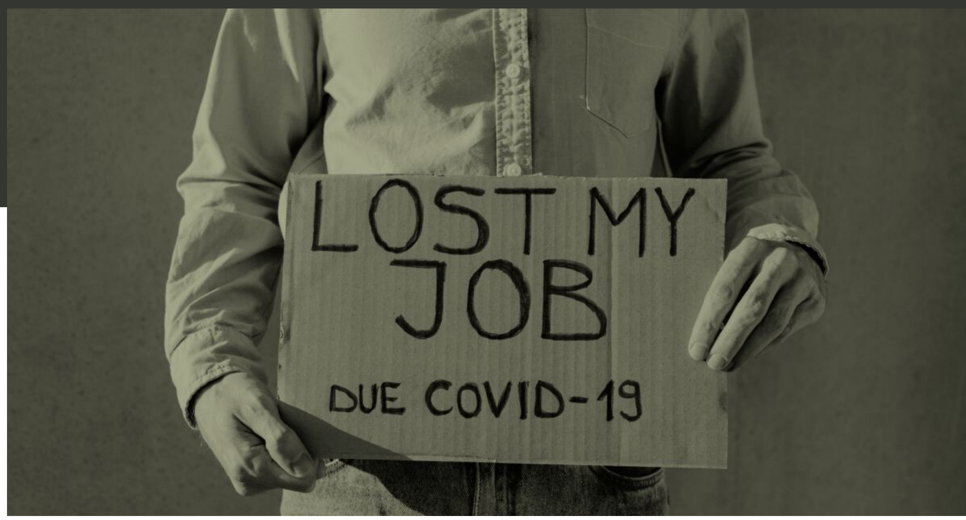
NONPROFITS: CALIFORNIA LEGISLATION

Unemployment Self-Insurance Fix For Nonprofits

07.24.20 | Linda J. Rosenthal, JD



The COVID-19 pandemic has hit U.S. employers and workers hard because of the unprecedented economic chaos along with mandatory stay-at-home orders. In normal times, the unemployment compensation laws and bureaucracy – a federal/state partnership – are a challenge to navigate.

In all American jurisdictions, 501(c)(3) organizations (along with government and tribal entities) may choose to opt out of the FUTA (Federal Unemployment Tax Act) system in favor of a self-insuring route. Under that alternative, the employer reimburses the state only for actual claims paid out to former workers."

Almost half of U.S. nonprofits self-insure because – generally – it achieves substantial cost savings over the FUTA route. But these are not normal times with normal levels of unemployment. And the icing on the cake is a "breathtakingly cruel" federal administrative rule issued in late April 2020 by the United States Department has made the dire self-insurance problem even worse.

Nonprofit leaders raised the alarm right away urging Congress to adopt at least one of several alternative possible fixes. Congress managed to step up to the plate earlier in July, wrangling bipartisan "unanimous consent" to pass S.4209, the Protecting Nonprofits from Catastrophic Cash Flow Strain Act.

Hailed as a "solid first step" by the nonprofit community, it is an important interim band-aid. This bill, passed on July 9th, finally reached the White House on July 22, 2020, and is expected to signed into law any time now. We'll update this post to reflect presidential action.

Unemployment Insurance & Nonprofits

The American system of unemployment compensation is a federal/state arrangement. The Federal Unemployment Tax Act (FUTA) is the original law that authorizes the government to tax businesses with employees "for the purpose of collecting revenue that is then allocated to state unemployment agencies and paid to [… eligible …] unemployed workers.

The state side of this partnership was "developed in each state alongside the federal unemployment tax. is commonly referred to as SUTA, the State Unemployment Tax Act. While it's generally referred to as the State Unemployment Tax Act (SUTA), some states have different names for it such as State Unemployment Insurance (SUI) or Reemployment Tax …."

SUTA is a "payroll tax employers are required to pay on behalf of their employees to their state unemployment fund." In most American jurisdictions, "employers are solely responsible for paying state unemployment insurance taxes to fund their state's unemployment insurance system." Most employers pay both a Federal and a state unemployment tax."

For the U.S. 501(c)(3) nonprofits that are permitted to opt out of this standard unemployment compensation arrangement, there are significant benefits; the main one is "cost savings. While savings numbers vary, most organizations can save between 30-50% a year." The key is that instead of paying into a tax system in advance, a "reimbursing employer" makes payments of actual employment compensation benefits only *when* layoffs occur.

Are there risks to electing this option? Yes, because it "provides no insurance against excessive unemployment claims …." Normally, in this risk-benefit analysis, it makes financial sense to make this choice. "The self-insured system allows for reasoned risk-benefit determinations and provides protections for different sizes and types of nonprofits…."

It's estimated that perhaps almost half of all nonprofits are "reimbursing" employers."

The Pandemic & the Problem

With the unemployment rates skyrocketing since March, this distinctly *not* normal employment situation has turned into a financial catastrophe for many nonprofits – above and beyond the overall COVID-19 disruption being felt all across the American economy.

"Congress's initial response to address this issue was to reduce the amounts that self-insured nonprofits owe by half under Section 2103 of the CARES Act." But "[t]his still creates a considerable hardship," according to Tiffany Gourley Carter In *Don't Let Senseless Unemployment Policies Sink Nonprofits—Act Now!* (May 8, 2020) in *The Nonprofit Quarterly*.

And in making rules to implement this new law, "the administration made this situation infinitely worse by forcing an unnecessary and burdensome double-reverse reimbursement structure" requiring self-insuring nonprofits to "first pay 100 percent of the costs of unemployment benefits paid to employees no longer working as a result of COVID-19. At some unknown time later, the nonprofits that are able to survive the cash crunch will receive a 50 percent reimbursement."

Some states had acted to mitigate the hardship, but this DOL "guidance also threatens to penalize states that worked to provide additional assistance to nonprofits—by withholding full federal support. See *DOL Issues Breathtakingly Cruel Guidance Inflicting Billions in Immediate Costs onto Charitable Organizations Struggling to Serve Their Communities* (April 28, 2020) National Council of Nonprofits

The Fix is Fixed … Sort Of

In urging action on this problem, many voices in the nonprofit community urged that the "…simplest, most straight-forward fix would be for Congress to hold self-insured nonprofits harmless for 100 percent of the costs that would be charged of their COVID-19 related unemployment insurance claims." That's why the Nonprofit Community Letter submitted to Congress calls for such legislation."

And while such "federal, 100 percent coverage is the best and most needed solution to protecting nonprofit employers and the people those nonprofits serve, other intermediary steps may be needed pending a full federal fix." Options included: (1) conforming state statutes to accept and use federal funding, various "hold harmless" arrangements, and delaying payment deadlines.

A group of six bipartisan senators introduced the Protecting Nonprofits from Catastrophic Cash Flow Strain Act. The Senate passed it by unanimous consent, followed by passage as well in the House of Representatives.

The National Council of Nonprofits issued a *Statement on House Passage of the Protecting Nonprofits from Catastrophic Cash Flow Strain Act* (July 9, 2020) characterizing the legislation this way: "It override[s] the Department of Labor's misguided, jobs-killing interpretation that was imposing economic burdens on charitable organizations that Congress never intended." Calling it a "…master stroke of bipartisanship," NCN further stroked Congress for acting "…to partially reduce the panic that many nonprofits will experience this month when dozens of states send out massive invoices for unemployment compensation costs. With nonprofit resources plummeting and demand for services rising, nonprofits that have already had to lay off employees could not bear the brunt of another huge bill to pay."

Conclusion

Noting that this "…legislation is not a complete solution to the problem of unemployment benefits costs that are dragging nonprofits down and forcing them to reduce services to the public," the National Council of Nonprofits calls it "a solid half-step toward the full solution needed." But "[t]here is also still much work to do to ensure that charitable nonprofits – our nation's third largest employer – can keep their employees on the payroll and can continue serving communities across the country."

The National Council of Nonprofits will host a briefing on the important matter on Wednesday, July 15, 2020 at 2pm EDT as part of its #Relief4Charities Week of Action. See here for more information.