

MINUTES

**MONTANA HOUSE OF REPRESENTATIVES
53rd LEGISLATURE - REGULAR SESSION**

SELECT COMMITTEE ON WORKERS' COMPENSATION

Call to Order: By CHAIRMAN CHASE HIBBARD, on February 10, 1993,
at 3:00 P.M.

ROLL CALL

Members Present:

Rep. Chase Hibbard, Chairman (R)
Rep. Jerry Driscoll, Vice Chairman (D)
Rep. Steve Benedict (R)
Rep. Ernest Bergsagel (R)
Rep. Vicki Cocchiarella (D)
Rep. David Ewer (D)

Members Excused: None

Members Absent: None

Staff Present: Susan Fox, Legislative Council
Evy Hendrickson, Committee Secretary

Please Note: These are summary minutes. Testimony and
discussion are paraphrased and condensed.

Committee Business Summary:

Hearing: HB 470, HB 455, HB 504
Executive Action: None

HEARING ON HB 361

Opening Statement by Sponsor:

CHAIRMAN HIBBARD opened the hearing on HB 361 to hear amendments dated February 8, 1993 which were presented before the committee heard the bill. Other amendments presented were addressed.

Nancy Butler, General Counsel for the State Fund, reviewed the amendments section by section. EXHIBIT 1

REP. DRISCOLL asked about the rehabilitation sections and a discussion ensued with Ms. Butler. Ms. Butler said they took out the reference to the workers' job pool which made the labor market either local or statewide. Rather than looking statewide to determine whether or not a worker is entitled to

rehabilitation benefits, it would be limited to a more of a local job market analysis. They would make the determination whether rehab benefits were payable.

HEARING ON HB 470

Opening Statement by Sponsor:

REP. JERRY DRISCOLL, House District 92, Billings, reviewed the bill and the amendments dated February 5, 1993. EXHIBIT 2 The intent of this bill is if a person represents to the public that he is an independent contractor and is working in the construction industry, he must have a policy.

Proponents' Testimony:

Bill Pierce, Montana Building Industry Association EXHIBIT 3

Harlee Thompson, Manager of Intermountain Truss, Helena, and a representative from the building industry association to the Coalition for Worker's Comp System Improvement (CWCSI) EXHIBIT 4

Lars Erickson, representing the Montana State Council of Carpenters, and a member of the CWCSI urged a do pass on HB 470.

Don Judge, representing the Montana AFL-CIO, urged a do pass on HB 470.

James Senrude, representing the CWCSI, said the bill gives the State Fund a much needed financial boost and urged a do pass on HB 470.

Carl Schweitzer, representing the Montana Contractors Association, supported the legislation.

Opponents' Testimony:

SEN. GARY FORRESTER, Senate District 49, Billings, agreed with the concept of the bill but not with the theory behind it. He said a fiscal note should be requested as the Department of Labor would need about eight auditors for this purpose. He then referred to a letter. EXHIBIT 5

Questions From Committee Members and Responses:

CHAIRMAN HIBBARD asked REP. DRISCOLL what the bill would do to the independent contractor who would no longer be exempt. REP. DRISCOLL said he could not be exempt and would have to have a policy. CHAIRMAN HIBBARD asked about the responsibility that occurs to either the general contractor or the ultimate employer

it would be whether or not they represented themselves to be an independent contractor or if they were an employee. They would have to prove that they represented themselves as an independent contractor. If they could prove that, then they violated the law by not getting a policy.

CHAIRMAN HIBBARD asked how many contractors this might bring into the system. REP. DRISCOLL said approximately 1,000.

REP. BENEDICT asked REP. DRISCOLL if the contractor could still apply for an exemption. REP. DRISCOLL said not under the amendments.

Closing by Sponsor:

REP. DRISCOLL said, with amendments presented with the bill, independent contractors could buy a policy from the State Fund based on \$900 a month payroll. If they don't buy a policy and they represent themselves to be an independent contractor, then they become an uninsured employer.

HEARING ON HB 455

Opening Statement by Sponsor: REP. JIM ELLIOTT, House District 51, Trout Creek, reviewed the bill and had no amendments.
EXHIBIT 6

Proponents' Testimony:

Don Judge, Montana State AFL-CIO, commended the sponsor for bringing forth the issue of immunity that is granted the employers of the state of Montana.

Russell Hill, representing the Montana Trial Lawyers' Association, spoke in favor of the bill. Mr. Hill said he had a concern with the repealer sections that repeal Montana statutes concerning uninsured employers and yet leave a void.

CHAIRMAN HIBBARD remarked that REP. GRIMES had signed this bill and asked REP. ELLIOTT if he had elected to support this bill in lieu of his own or if he is bringing his own bill forward. REP. ELLIOTT said he would have to talk to REP. GRIMES about that.

Opponents' Testimony: None

Closing by Sponsor: REP. ELLIOTT said SENATOR CRIPPEN had also signed onto this bill. The independent insurance agents supported the bill in concept; small businesses, labor and the trial lawyers also like it.

The committee may want to consider amending the bill to put damage award limits in and exempt the employer who hires an employee five days a year; only people who hire less than five people fulltime could opt out of the workers' comp act.

Informational Testimony: None

CHAIRMAN HIBBARD closed the hearing on HB 455.

HEARING ON HB 504

Opening Statement by Sponsor: REP. BENEDICT reviewed HB 504, a product of the Joint Select Committee on Workers' Compensation. EXHIBITS 7 and 8

Proponents' Testimony: None

Opponents' Testimony:

Mr. George Wood, Executive Secretary of Montana Insurers Association, said they strongly oppose the payroll tax. This tax has been paid since 1987, and the payments from the 55 employers in this group represent 25% of the payroll tax paid. For the employers it's a 357% increase in the payroll tax. Mr. Wood called the committee's attention to line 10, page 6 of the bill, the stricken language. He said this was a legislative promise to them at the time the payroll tax was instituted, and this promise is not being fulfilled. He recommended a do not pass.

James Tutwiler, representing the Montana Chamber of Commerce, explained their opposition to this bill. The bill repeals the state's subsidy of workers' compensation and subsidizes on the backs of employers by continuing a payroll tax.

Mr. Tutwiler reviewed the bonding problems and said there would be a more reasonable consideration if everyone addressed the new fund in such a way as to instill confidence and some predictability into the work comp system.

Riley Johnson, National Federation of Independent Business (NFIB), gave the results of the 8,600 members surveyed this past fall. With a 43% return, 65% said no to the one-on-one tax, 24% said yes and 11% were undecided. Mr. Johnson reiterated the comments made by Mr. Tutwiler. He also said the small family corporations will get this tax twice with the payroll tax and the salary tax. On the same ballot the members were asked if they want employee participation in some form of workers comp system. This vote came out 75% yes, 20% no and 4% undecided.

Bob Olsen, Montana Hospital Association, said they were opposed

to this bill as it would drive up the cost of health care.

Steve Kirkwood, representing the **Montana Auto Dealers Association**, a trade association of 137 of Montana franchises, opposed HB 504.

Mike Micone, representing the **Montana Motor Carriers' Association**, opposed the bill.

Charles Brooks, **Montana Retailers Association**, said for a number of reasons stated by others the Association is very much opposed to the 1% tax on retailers as well as their employees.

Don Judge, **AFL-CIO**, said they were opposed for the same reasons as stated previously.

John Lalane, **Montana Federation of Teachers and Montana Federation of State Employees**, said they were opposed to the bill for many of the same reasons stated above.

Jim Senrude, representing the **CWCSI**, said they wanted to go on record as opposing the bill.

Questions From Committee Members and Responses:

REP. DRISCOLL stated that the old debt is a fact but nobody wants to pay for it. If something isn't done, those injured workers are going to go back and sue the employer they were working for at the time of the injury.

Mr. Wood said this is an issue that comes up every session. Everyone seems to feel this is a debt of the employers and employees. Lottery, coal tax, and the general fund have all been suggested, but the answer is always "there is no money."

Mr. Micone said that until such time as the working community is assured that the legislature has dealt with the problem and that the future of workers' compensation in this state is corrected, he didn't think there would be any movement on the part of anyone to agree to an additional tax. He suggested the legislature take a look at resolving the problem, making the structure secure and stable and then decide whether or not to increase taxes.

Mr. Senrude asked if it had been suggested to take coal tax severance money and repay that out of the new fund.

CHAIRMAN HIBBARD said that, contrary to much opinion, the coal trust fund is leveraged to the maximum for state borrowing and is not available.

Casey Emerson with **King Tool, Inc.** from **Bozeman** said to correct the problems with the system.

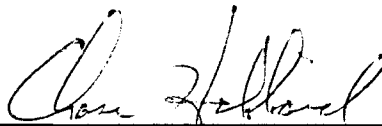
CHAIRMAN HIBBARD asked REP. EWER if he intended to submit any amendments. REP. EWER said the bill, as it now stands, would have a 1% tax. He said he will soon have amendments for the committee's consideration that will have other payroll tax rates.

Closing by Sponsor: REP. BENEDICT closed.

CHAIRMAN HIBBARD announced that HB 487 by REP. BRANDEWIE, HB 456 by REP. BENEDICT, and HB 511 by CHAIRMAN HIBBARD would be heard on Friday, February 10.

ADJOURNMENT

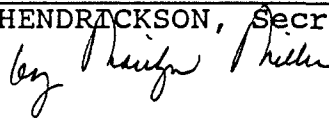
Adjournment: 5:00 p.m.



REP. CHASE HIBBARD, Chairman



EVY HENDRICKSON, Secretary



CH/eh

HOUSE OF REPRESENTATIVES
53RD LEGISLATURE - 1993
SELECT COMMITTEE ON WORKERS COMPENSATION

ROLL CALL

DATE _____

7-10-93

[illegible]

HR:1993

wp.rollcall.man

Amendments to House Bill No. 361
First Reading Copy

Henry Dutton -
EXHIBIT 1
DATE 2-10-93
HB _____

Requested by Representative Hibbard
For the Select Committee on Workers' Compensation

Prepared by Paul Verdon
February 8, 1993

1. Title, line 18.
Following: "WORKER;"
Strike: remainder of line 18
2. Page 4, lines 24 and 25.
Strike: "diagnostic evidence, substantiated by clinical findings"
Insert: "verifiable findings demonstrated by accepted diagnostic procedures"
3. Page 5, line 1.
Strike: "clinical"
Insert: "verifiable"
4. Page 14, line 25.
Strike: "subsection"
Insert: "subsections"
Following: "(4)"
Insert: "and (5)"
5. Page 15, line 16.
Following: line 15
Insert: "(4) If the treating physician releases a worker to return to the same position, the worker is no longer eligible for temporary total disability, regardless of availability of employment."
Renummer: subsequent subsections
6. Page 15, lines 17 and 18.
Following: "the" on line 17
Strike: remainder of line 17 through "the" on line 18
7. Page 17, line 13 and 14.
Strike: ", as determined after a vocational rehabilitation evaluation"
8. Page 22, lines 12 and 13.
Strike: "wage supplement,"
9. Page 22, line 16.
Following: "~~award~~,"
Insert: ", any impairment award,"
10. Page 24, line 20.
Following: "~~less~~"
Insert: "or \$20,000, whichever is less"

EXHIBIT

DATE 2/10/93

HB 361

11. Page 25, lines 4 through 7.
Strike: subsection (3) in its entirety
Renumber: subsequent subsections

12. Page 26, line 2.
Strike: "subsection"
Insert: "subsections"
Strike: "(4)"
Insert: "(2) and (3)"

13. Page 26, line 11.
Strike: "or 7%, whichever is greater"

14. Page 29, lines 4 through 16.
Strike: subsection (7) in its entirety

15. Page 30, lines 10 and 11.
Strike: "in the worker's local or in the statewide job pool"

16. Page 32, lines 7 through 11.
Strike: subsection (2) in its entirety
Renumber: subsequent subsections

Amendments to House Bill No. 470
First Reading Copy

Requested by Representative Driscoll
For the Committee on Workers' Compensation

Prepared by Eddy McClure
February 5, 1993

1. Title, line 9.
Following: "AMENDING"
Strike: "SECTION"
Insert: "SECTIONS"
Following: "39-71-401"
Insert: "AND 39-71-405"
2. Page 2, line 5.
Following: "employment"
Insert: ", in a position other than a position in a construction industry,"
3. Page 2, line 9.
Following: "partnership,"
Insert: "in a position other than a position in a construction industry,"
4. Page 3, lines 21 and 22.
Following: "contractor"
Strike: remainder of line 21 through "services" on line 22
5. Page 3, line 25.
Following: "for"
Strike: "a personal"
6. Page 4, line 1.
Following: "Act"
Insert: ", unless the sole proprietor or partner is contracting for construction industry services"
7. Page 5, line 4.
Following: "chapter"
Insert: "if the officer does not work in a construction industry"
8. Page 6, line 18.
Following: line 17
Insert: "Section 2. Section 39-71-405, MCA, is amended to read:
"39-71-405. Liability of employer who contracts work out.
(1) An employer who contracts with an independent contractor, except an independent contractor working in a construction industry, to have work performed of a kind which is a regular or a recurrent part of the work of the trade, business, occupation, or profession of such employer is liable for the payment of benefits under this chapter to the employees of the contractor if the contractor has not properly complied with the coverage

requirements of the Worker's Compensation Act. Any insurer who becomes liable for payment of benefits may recover the amount of benefits paid and to be paid and necessary expenses from the contractor primarily liable therein.

(2) Where an employer contracts to have any work to be done by a contractor other than a contractor working in a construction industry or an independent contractor, and the work so contracted to be done is a part or process in the trade or business of the employer, then the employer is liable to pay all benefits under this chapter to the same extent as if the work were done without the intervention of the contractor, and the work so contracted to be done shall not be construed to be casual employment. Where an employer contracts work to be done as specified in this subsection, the contractor and the contractor's employees shall come under that plan of compensation adopted by the employer.

(3) Where an employer contracts any work to be done, wholly or in part for the employer, by an independent contractor, where the work so contracted to be done is casual employment as to such employer, then the contractor shall become the employer for the purposes of this chapter."

{ Internal References to 39-71-405: None. }

Renumber: subsequent sections

9. Page 6, lines 23 and 24.

Strike: ":" through (a) on line 24

10. Page 6, line 25.

Following: "contractor"

Strike: "; and"

Insert: "if the contractor does not work in a construction industry."

11. Page 7, lines 1 through 7.

Strike: subsection (b) in its entirety

12. Page 7, line 12 and line 14.

Following: "section"

Strike: "2"

Insert: "3"

EXHIBIT 2
DATE 2/10/93
HB 470

Homebuilders Assoc. of Billings
252-7533

S.W. Montana Home Builders Assoc.
585-8181

Great Falls Homebuilders Assoc.
452-HOME



EXHIBIT 3
DATE 2-10-93

Flathead Home Builders Assn
752-2522

Missoula Chapter of NAHB
273-0314

Helena Chapter of NAHB
449-7275

Nancy Lien Griffin, Executive Director

Suite 4D Power Block Building • Helena, Montana 59601 • (406) 442-4479

Mr. Chairman, Ladies & Gentlemen of the Committee:

For the record, I am Bill Pierce, Chairman of the Legislative Committee of the Montana Building Industry Association. For several years our association has supported elimination of the much abused independent contractor exemption. This legislation, which was passed last session, but vetoed by the Governor, has been introduced this session by Rep. Driscoll at the request of the Carpenter's Union and our association.

Some confusion in bill drafting resulted in the addition of the amendments proposed by Rep. Driscoll. Without the amendments the bill does not meet the intent of total elimination of the exemption which we support. Upon review of the amendments we find a couple of minor technical errors and I have submitted some additional amendments.

We find ourselves often at a crossroads with other members of our industry who rely on the exemption to cut business costs. The building industry has always been a relatively dangerous profession, and while efforts are constantly being made to improve safety performance, disabling accidents will always be a major concern. The industry is also characterized by the extensive use of subcontracting.

The general contractor theoretically needs to check for a current "independent contractors' certificate" for every individual on the construction site who claims such status. Logistically, such a procedure is virtually impossible with multiple construction sites and a daily turnover in some site personnel. When an injury occurs, the worker is almost always ruled an employee and not an independent contractor. We are concerned both for adequate worker coverage and liability risk to general contractors and homeowners. We find it is difficult to propose such legislation for members of our own industry, but we adamantly believe that it is time to "bite the bullet" and take responsibility for the cleanup of our industry.

Please let me make it clear to the committee that this is our industry's attempt to make changes within our own industry, and the intent of this legislation is to eliminate the independent contractor exemption only for the construction industry. A requirement for workers' compensation insurance coverage for all in the construction trades, is a reasonable and justified protection for workers, families, businesses, and homeowners.

We urge a Do Pass for HB 470, a much needed piece of worker's comp reform.

HB 470 with Amendments
Elimination of Independent Contractor Exemption for Construction Industry

Recommend:
Do Pass

Mr. Chairman, Ladies & Gentlemen of the Committee:

I am Harlee Thompson, manager of Intermountain Truss in Helena, and a representative from the building industry association to the Coalition for Worker's Comp System Improvement (CWCSI).

For the past year the Coalition has conducted an extensive study of Work Comp problems. In our analysis it has come to light that one of the major problems is the uninsured independent contractor. In many instances this "independent" contractor becomes an employee upon injury. This is a worker that constitutes a liability for the work comp system without payment of premium. It is common knowledge in the construction industry that an "employee" is an "independent contractor" that just had an injury.

In a recent OSHA survey of 360 Montana employers providing statistics in their OSHA logs, the construction industry has the highest incident rate of any other industry, at 17.5 accidents per 100 employees. The incident rate for specialty trades in the construction industry rose from 13.4 incidents per 100 in 1990 to 18.1 incidents in 1991.¹ Other states, including Oregon, have recognized the problem, and adopted system reforms which eliminated exemptions for the construction industry. The result has been an increase in revenues to cover injury liabilities.

Elimination of the abused independent contractors exemption is proposed specifically for the construction industry. Current practice establishes 20 questions which determine independent contractor status. In our experience it is virtually impossible, because of the interaction of the many subcontractors and special trades contractors on a single building site, to answer "no" to all questions. The courts then have passed routine rulings which determine the injured claimant as an employee.

This legislation is an important part of the reform necessary for practical improvement to the Worker's Comp system. We urge a do pass for HB 470.

¹Interesting Facts from 1991 OSHA Survey", Montana Department of Labor.

State of Montana

Stan Stephens, Governor

EXHIBIT 5

DATE 3-10-93

HB 470



Department of Revenue

Denis Adams, Director

Income and
Miscellaneous Tax Division

Jeff Miller, Administrator

October 4, 1991

Representative Gary Forrester
2527 Gardiner St. R 8
Billings, Montana 59101

Dear Representative Forrester:

As we have discussed, the influx of contractors into the Billings area presents compliance issues for a number of agencies. Taxes and fees are potentially due for motor vehicles, unemployment, worker's compensation insurance, building permits, contractors licenses, and of course, with the Department of Revenue in the form of employer withholding and individual income tax.

The Department is in an unusual position because as of today, **no reports related to this work are due.** Individual Income Tax returns are not due until April 15, 1992. The first Employer withholding quarterly reports covering this particular activity are not due until the end of this month. However, given the scope of this activity we intend to take an unusual step. We are beginning withholding audits before the reports are due. This audit project was begun by my Billings Field Office more than a month ago. They have identified an initial pool of 49 contractors as potential audit candidates. Research to date has included a review of building permits and contractor's licenses and Department records to identify owners of these businesses. Of the 49, we have found only 13 who are registered and withholding individual income tax.

We have also invited the Department of Labor to join in a cooperative audit effort. Five contractors have been scheduled for joint audits next week, October 7th - 11th. If our audit determines a worker is an employee, withholding, unemployment, and worker's compensation insurance are all due. The joint audits will include both registered and unregistered employers as one of the businesses registered has as many as 40 crews working. In addition to the joint audits, we have scheduled a total of 18 other employer audits. Based on the results of this initial effort, we will decide what further efforts are warranted. I'll be back in touch with you when I have some results I can report.

Sincerely

A handwritten signature in cursive script, appearing to read "Jeff Miller".

Jeff Miller, Administrator

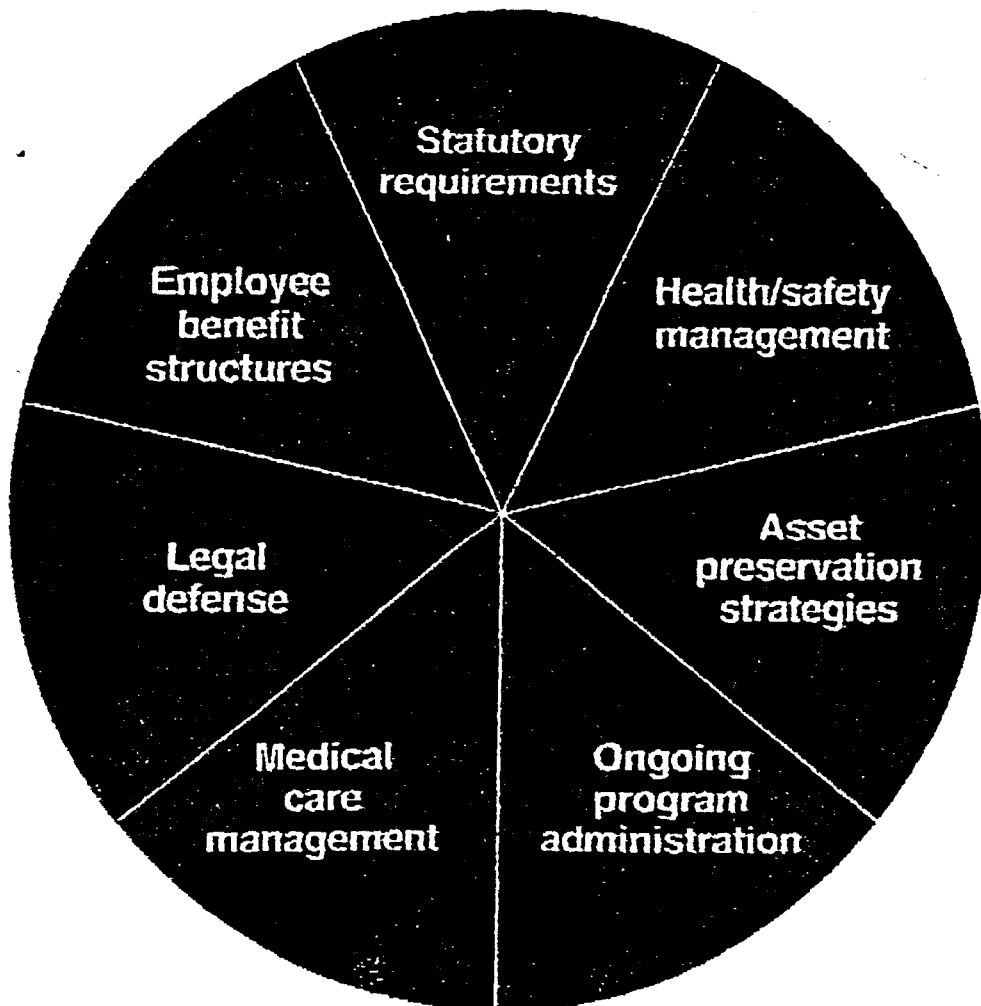
Neil Rabor

DATE 2-10-93

HB 455

Elliott'

A Legal Defense Solution



Better Employee Benefits at Lower Cost

SOUTH CAROLINA WORKERS' COMPENSATION COMMISSION

~~RECEIVED~~ NOTICE TO REJECT

This form is required if an employer desires to exempt his business from the provisions of the South Carolina Workers' Compensation Act.

Date: _____, 19____.

To the Employees of the Undersigned and the South Carolina Workers' Compensation Commission:

The undersigned employer rejects the terms, conditions and provisions of the S.C. Workers' Compensation Act and elects to pay damages for personal injuries received by employees of this business under the common law and statutes of South Carolina, as modified by the provisions of the Workers' Compensation Act.

As provided by law (Section 42-1-340), a copy of this notice must be posted in the shop, plant, office, room or place where the employee(s) is employed, or by personal service upon the employee(s).

This rejection takes effect thirty (30) days after the date it is received by the South Carolina Workers' Compensation Commission.

*** PLEASE PRINT OR TYPE ALL INFORMATION *** ORIGINAL SIGNATURES REQUIRED ***

EMPLOYER

SWORN TO AND SUBSCRIBED BEFORE ME

at _____

this _____ day of _____, 19____

Notary Public for South Carolina

My Commission Expires: _____

For Official Use Only:

Date Received: _____

Effective Date: _____

Approved By: _____

Telephone Number: _____

Reference Summary:

Section 42-1-310

Section 42-1-340

Section 42-1-310

Name of Business (Legal Name)

Federal Employer I.D. #

Street Address

Post Office Box

City

State

Zip Code

By: _____

Name and Title

Area Code

Telephone Number

Signature of Employer Official

Date

For more information about the provisions of these Sections and this form, contact:

South Carolina Workers'
Compensation Commission
Coverage & Compliance Department
Post Office Box 1715
Columbia, S.C. 29202-1715
(803) 737-5708

- ▶ Protect the rights of the employer while reducing its costs; and
- ▶ Assist the employer in preserving assets from groundless claims.

The Benefits:

SCFA's Employer/Employee Partnership Program will provide many substantial benefits including:

Statutory Requirements

- ▶ Develop proper notification and postings for your employees as required by the South Carolina Workers' Compensation Act.
- ▶ Create policies and procedures to protect employers from statutory employment issues.

Health/Safety Management

- ▶ Prepare up-to-date policy manuals to cover safety in the workplace and employee orientation and training, including:
 - (1) "Management Guidebook for Employment and Preventive Health and Safety Procedures;"
 - (2) "Employees Guide for Safety and Health";
 - (3) "Employees Health and Safety Policy Manual".
- ▶ Review and revise if necessary your existing policy manuals and materials with respect to safety issues.
- ▶ Analyze incident/accident history and determine your company's actual loss experience in order to:
 - (1) Project your anticipated future injury expectations, and
 - (2) Establish your estimated cost savings.
- ▶ Establish specific procedures for dealing with incidents of workplace injury.
- ▶ Train designated supervisory employees to implement these procedures.
- ▶ Counsel supervisors and managers on the program's stated health and safety policies on an on-going basis.
- ▶ Develop employment practices to address your employee's physical and mental ability to perform his job (to comply with the new Americans With Disabilities Act).
- ▶ Create a detailed and specific communicable disease education program for your employees.

EDM 3.1 6
 DATE 2/10/93
 HQ 455

SOUTH CAROLINA FINANCIAL ALTERNATIVES, INC. (SCFA) can provide your company with relief from the turmoil caused by the "reform" of the South Carolina Workers' Compensation Act.

The Problem:

The cost of participating in the South Carolina Workers' Compensation system is by far the largest uncontrollable business expense for a South Carolina employer. Traditional sources of workers' compensation insurance have either abandoned the market, refused to issue future protective coverage, or have raised rates substantially. The inefficiency of this government-run program has resulted in low quality protection for employees and ever-increasing costs to employers. The bottom line has become reduced profits and fewer jobs.

Now, many companies are electing out of the workers' compensation system-to be "non-subscribers" under the Act. If this election is made, an employer becomes potentially liable for unlimited damages for each claim made by an employee. When a company makes this election without an adequate solution, it is like jumping out of a burning building before the fire department has arrived with a safety net.

The Solution:

SCFA has been formed to provide a viable solution for employers which is better than either the high cost of participating in the state's workers' compensation system or the excessive liability of simply "going bare." SCFA's Employer/Employee Partnership Program provides;

- ▶ Better benefits and increased safety in the workplace for employees at approximately 50% less cost to the employer than workers' compensation premiums.
- ▶ Guidance in meeting the statutory requirements for a non-subscribing employer.
- ▶ Limitation of an employer's risks through the use of sophisticated planning and management techniques.

The Goals:

SCFA works to establish a cooperative relationship between employers and employees. The goals of the SCFA program are to minimize injury in the workplace and eliminate any adversarial relationship between the employer and the injured employee. The result will be better treatment for the employees and less risk of litigation for the employer. SCFA will work with any employer to set up a thorough and systematic program to:

- ▶ Improve the safety of the workplace for all employees;
- ▶ Enhance both the quality and the cost efficiency of medical treatment for a legitimately injured worker;

EXHIBIT 6
DATE 2/10/93
HS 455

- ▶ Protect the rights of the employer while reducing its costs; and
- ▶ Assist the employer in preserving assets from groundless claims.

The Benefits:

SCFA's Employer/Employee Partnership Program will provide many substantial benefits including:

Statutory Requirements

- ▶ Develop proper notification and postings for your employees as required by the South Carolina Workers' Compensation Act.
- ▶ Create policies and procedures to protect employers from statutory employment issues.

Health/Safety Management

- ▶ Prepare up-to-date policy manuals to cover safety in the workplace and employee orientation and training, including:
 - (1) "Management Guidebook for Employment and Preventive Health and Safety Procedures;"
 - (2) "Employees Guide for Safety and Health";
 - (3) "Employees Health and Safety Policy Manual".
- ▶ Review and revise if necessary your existing policy manuals and materials with respect to safety issues.
- ▶ Analyze incident/accident history and determine your company's actual loss experience in order to:
 - (1) Project your anticipated future injury expectations, and
 - (2) Establish your estimated cost savings.
- ▶ Establish specific procedures for dealing with incidents of workplace injury.
- ▶ Train designated supervisory employees to implement these procedures.
- ▶ Counsel supervisors and managers on the program's stated health and safety policies on an on-going basis.
- ▶ Develop employment practices to address your employee's physical and mental ability to perform his job (to comply with the new Americans With Disabilities Act).
- ▶ Create a detailed and specific communicable disease education program for your employees.

EXHIBIT 6
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42455

Asset Preservation Strategies

- ▶ Reduce the risks for the employer and its owners through asset preservation and business planning strategies.
- ▶ Provide substantial estate tax savings for business owners and key executives.

Ongoing Program Administration

- ▶ Establish procedures for documenting workplace injuries and the maintenance of necessary data and information.
- ▶ Create a comprehensive program for responding to potential and actual litigation situations. This includes formats for recordkeeping, formal responses and related documentation.

Medical Care Management

- ▶ Establish a medical management system for handling all work related injuries or illnesses, as well as providing preventive health information.
- ▶ Identify a network of physicians and/or clinics to provide quality, cost efficient medical care.
- ▶ Implement procedures to assist the injured or disabled workers with the goal of reintegrating them into the workplace.

Legal Defense

- ▶ Provide assistance to legal professionals in the defense of claims which cannot be resolved after diligent effort.

Employee Benefit Structures

- ▶ Reduce the potential catastrophic risks of non-subscription through the recommended use of various insurance products available from a choice of insurance companies. To discourage abusive claims, insurance proceeds reimburse the employer rather than make direct payments to employees. SCFA cooperates with insurance professionals to help create the best protection available.

The Results:

SCFA's Employer/Employee Partnership Program allows the employer to regain control over the costs of providing quality care and a safe workplace for his valuable employees.

For information contact Paul Harper
at South Carolina Financial Alternatives, Inc.,
501 E. McBee Ave. Suite 106 Greenville, SC 29601, (803) 242-1727

EXHIBIT 6
DATE 2/10/93
40 455

PREVENTIVE RISK MANAGEMENT
OF
EMPLOYEE INJURIES

Look at your year-end "Income and Expense Statement!"

Is your workers' compensation premium one of the highest expenses you incur? What is an alternative?

The objectives of Preventive Risk Management are very simple
Internal control and efficient use of resources!

The team of experts of South Carolina Financial Alternatives, Inc. provides comprehensive analysis, development, and installation of a Preventive Risk Management Program for cost-effective delivery of your goods and services to your clients.

South Carolina Financial Alternatives, Inc. provides its clients with Risk Management assistance in finding solutions to specific problems and to offer you comprehensive support services for:

- *Alternative solutions to risk problems, using methods designed to reveal "all exposure to risk."
- *Analysis of the effect of those risks on the company or facility to measure their relative severity.
- * Application of approved techniques of risk handling.
- *Improvement in the efficiency of employment procedures and thus employee morale through risk management.
- *Reduction of employee injury claims, employment claims, and aid in the defense against other types of claims your business may experience.

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"THE RISK MANAGEMENT APPROACH"

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NON-SUBSCRIBERS

Non-participants to the South Carolina Workers' Compensation act are spared the multi-thousand dollar premiums customarily charged for workers' compensation coverage. In order to recover on a claim for employee injury, from a non-subscriber, an employee must prove:

1. The injury occurred while he/she was acting within the course and scope of his/her employment;
2. That the injury is attributable to the negligence of the employer.

As indicated above, the burden is on the employee to prove that negligence of the employer caused the injury. The common employer negligence claims by injured employees of non-subscribers include the following allegations:

"The employer was negligent in failing to maintain adequate staff to achieve the job goal;"

"The employer was negligent in failing to maintain safe premises and working conditions for employees;"

"The employer was negligent in failing to have or to properly maintain the necessary equipment to complete the job in a safe and efficient manner;"

"A negligent act was committed by a supervisor or fellow employee (such acts are attributable to the employer)."

South Carolina Financial Alternatives, Inc. offers a programmatic and systematic approach to risk handling, including assessment, documentation, orientation and training, and materials, all designed to reduce and/or eliminate employee injuries.

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Initial consultations are provided each potential client to assess need, to determine approximate costs, and to advise the client on the viability of the Program. Each Program is structured, as appropriate, in phases to provide the client the flexibility and control necessary for a smooth transition. Changes in client circumstances are accommodated in the Program.

Implementation includes:

1. Design and production of Management Guide to Preventive Risk Management, with appropriate forms.
2. Design and production of Employee Policies and Guide to Health and Safety,, with appropriate forms and illustrations.
3. Survey and recommendations for on premises/off premises safety consistency measures.
4. Supervisor Program orientation, as appropriate to your operation.
5. Training in incident handling, documentation, and resolution.
6. Continuing risk analysis and Program review on an annual basis, and as you may request.
7. Administration and consultation in incident matters on which you may request assistance.

The employee injury risk is substantially reduced by tightening an employer's practices in order to give the employer the best chances of defense against an injury allegation.

Steps are taken to assure that proper training and documentation is provided all employees, while paying particular attention to job description.

Careful attention is given to employment applications, paying particular attention to references listed, the reasons for leaving former employment, and correct ways of obtaining the information. Properly obtained information will often reveal whether a prospective employee is a "chronic complainer," has filed for questionable injury benefits before, is trustworthy and dependable, and is physically able to perform the job under consideration.

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Attention is given to an employee's medical history and the injuries the employee is said to have suffered. Diligent inquiry is made into all such injuries prior to hiring such employees, again to determine physical and mental capability to perform the job.

With no Preventive Risk Management Program in place, you may be at the mercy of the Plaintiff. As in personal health, preventive measures are superior to and far less costly than treating an issue after it has arisen.

For more information on the services offered by South Carolina Financial Alternatives, Inc., please contact our office at the address enclosed or call us at (803) 242-1727.

We will be pleased to arrange a time for presentation of the Program.

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**SOUTH CAROLINA EMPLOYER/EMPLOYEE PARTNERSHIP PROGRAM
SYSTEMATIC APPROACH TO LEGAL PROTECTION
For the Non-Subscriber Employer**

Pre-Post Employment	Orientation/Training Materials	Employee Policies/Procedures and Handbook
<ul style="list-style-type: none"> *Application *Medical Evaluation *Drug testing *Criminal history check *Background check *Release of Medical records *Release of Employment records *License checks *Checklists *Job Descriptions *Procedures/Practices 	<ul style="list-style-type: none"> *Management Guide *Guide to Health and Safety *Training materials *Demonstration materials *Procedures/Practices *Checklists *Acknowledgements 	<ul style="list-style-type: none"> *Employee Handbook *Policies relating to safety *Policies/Procedures relating to injury reporting/handling *Employee Benefits *Incentive Programs *ERISA Plans *Statutory Notices

Prospective Healthcare Management	Litigation and Defense Management
<ul style="list-style-type: none"> *Policies/Procedures related to injury handling *Forms relating to injury reporting *Off-site Employer Medical Director *Arrangements made with qualified physician *PPO/TPA *Records, audit and reports *Return to work program *Fraud Control 	<ul style="list-style-type: none"> *Provide assistance in the areas of documentation, expert testimony, and evidentiary production as may be required *Handle inquiries from employee's attorney *Defend lawsuits arising from employee injury

NOTE: The Preventive Risk Management Program's forms, procedures and materials are intended to predictably prevent legal consequences. The Program assists in the prevention of consequences that may arise from EEOC, Title 7 of the Civil Rights Act, OSHA, Civil Rights Act of 1991, the Americans with Disabilities Act, and other state/federal discrimination laws as they may apply to a non-subscribing employer.

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S.C. EMPLOYER/EMPLOYEE PARTNERSHIP PROGRAM

STAGES OF EMPLOYMENT AND INJURY PREVENTION

Pre-Post Employment Screening	Orientation and Training	Employment Policies Procedures Relating to Safety, Injury and Benefits (Employee Handbook)
Keep problematic potential medically costly or claim intensive employees from beginning employment.	Shifts the responsibility to the employee for their own safety and that of their fellow employees, by changing the employees' mind set through Health and Safety Education. Injuries can be prevented. If there are no injuries, productivity increases.	Establishes regulations relating to reporting and handling of injury, to include benefit description. Economic losses are limited at this stage through fraud control.

Prospective Healthcare Management for Employee Benefits

Litigation and Defense Management

Economic control is essential at this
stage through directing and controlling
medical costs. Reduced medical costs
through utilization review and return
to work programs. This stage is also
important to control fraud.

Economic control through directed legal
professionals in the defense of employee
injury litigation

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CONTRASTING INJURY PROCESSES

CLAIMS*	NON-SUBSCRIBER	SUBSCRIBER
1. Reporting	Incident report	Employer's First Report of Injury filed with the SCWCC and insurance companies
2. Temporary disability	Employer discretion	Prescribed by statute
3. Permanent disability	Employer discretion	Prescribed by statute
4. Medical expenses	Employer discretion	100% mandatory
5. Miscellaneous expense	As incurred	As incurred
6. Litigation	Civil negligence	Handled by the SCWCC or trial de novo, if employee is dissatisfied
7. Rehabilitation	Employer discretion	Option, based on viability
8. Light duty program	Employer discretion	Not mandated but may be offered by employer
9. Termination of benefits	Employer discretion	SCWCC/Carrier discretion as allowed by statute
10. Denial of claims	Employer discretion	Outlined by statute
11. Questionable claim	Employer discretion	Payment directed by Workers' Compensation Commission

* As a non-subscriber, the term "claim", as other terms of art of the insurance industry, is not used. This exhibit is a comparison of claim processes between the workers' compensation system and a non-subscriber employer.

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**J. Tommy Sautter, CPCU, ARM
Program Consultant**

Mr. Sautter holds national certification as a Charter Property Casualty Underwriter (CPCU), Associate in Risk Management (ARM), and is licensed by the State of Texas as a Risk Manager and All Lines Claims Adjuster. From 1968 to 1978, Mr. Sautter served as Board Representative to the Texas Industrial Accident Board for a major insurance company and has over twenty years experience in corporate and industrial risk management and insurance. Mr. Sautter has assisted companies with employee injury risk retention programs, including non-subscription issues, since 1978.

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LEGAL DEFENSE RECORD

S. C. Financial Alternatives, Inc. (SCFA), under exclusive contract with Management Risk Services (MRS), a Texas company, offers the Employer/Employee Partnership Program to South Carolina employers.

The Program has a strong record of success in the prevention of both on-the-job injury and Plaintiff's counsel involvement during its thirteenth (13) year history of assisting non-subscriber employers in Texas. Since the program's first introduction in 1978, its clients have returned as little as 80% and as much as 90% (including our fees) of their average annual workers' compensation premium to their bottom line, while providing their employees a true benefit when legitimately injured on the job. Fraudulent occurrences are eliminated, full control is returned to the employer's hands, profit/expense margins of the insurance industry are removed, and medical treatment is controlled by physician and facility designation, eliminating "doctor-shopping" by the employee.

MRS's program is designed around a client's operations and loss history to provide an immediate legal defense against fraud and malingering while addressing attendant issues necessary to reduce legitimate injury. Included are issues other than negligence such as wrongful discharge, involuntary discrimination, the Americans with Disability Act (ADA), AIDS/Communicable Disease and substance abuse in the workplace. Emphasis is placed on training supervisors in the work setting in all areas of employee responsibility. Employees are also educated in their responsibilities and duties, and thorough documentation is accomplished. It is a program of management efficiency which helps reduce the time spent on personnel and administrative matters.

Following the implementation of the risk management and education/training program, the client's success has come from ongoing services of (1) continued program monitoring; (2) medical treatment and cost management; and (3) legal defense from the moment of involvement by a Plaintiff attorney. Although risk of litigation is ever present for all employers, the legal defense history with over 1,100 employers and approximately 500,000 employees during the past thirteen (13) years has been extremely successful.

Although clients have had numerous inquiries from the Plaintiff's bar, only eleven (11) of those inquiries have proceeded past the initial contact. In each of these eleven (11) cases a personal injury lawsuit was filed. In nine (9) cases, litigation was dismissed with prejudice by the Plaintiff either prior to or immediately following the first deposition. In each case, no settlement was offered or rendered by the clients. The remaining two (2) cases are briefly described as follows:

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H. The Plan and the Employee: Voluntarily providing Plan Benefits reduces the financial burden an injury places on an employee and his/her family. This improves employee relations, and reduces employee incentive and financial need to bring a negligence suit; this can be a real psychological advantage for the employer. Meeting ERISA gives your injury benefit program structure and predictability; and it gives you something to hand your employees when you "take away" their comp!

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ERISA And the Non-Subscribing Employer

- A. When an ERISA Plan is needed: If a non-subscriber employer pays for any program (including AD&D insurance) which provides employee medical, surgical or hospital care benefits, or benefits in event of accident or disability, the program and the employer are covered by ERISA.
- B. South Carolina law claims pre-empted by ERISA: A proper written ERISA plan (a "Plan") can protect you against employee state common law claims for negligence or gross negligence in handling injury benefits, fraud, intentional infliction of emotional distress, misrepresentation of injury benefits, breach of contract, breach of fiduciary duty, breach of duty of good faith and fair dealing, and other state common law claims. Today, ERISA does not pre-empt workplace personal injury negligence claims; it will pre-empt claims for negligence in handling the employer's injury benefit program, granting and withholding benefits, representing, explaining and handling the accident (AD&D) insurance policy, etc. Absence of a Plan under ERISA can leave you open to these state common law claims.
- C. South Carolina statutes pre-empted by ERISA: A proper written ERISA Plan can protect you against state statutory claims under the S.C. Insurance Code (such as unfair insurance practices and wrongful withholding of benefits). Absence of a Plan under ERISA can leave you open to these state statutory claims.
- D. Why an ERISA Plan is needed: There are simple notice and filing requirements under ERISA, which require written documentation. They are not complex for small employers. However, if the employer has no written Plan, or has a written Plan without proper filing, it is subject to administrative penalties under ERISA, not to exceed \$1,000 per day. A written Summary Plan Description must be communicated to each participating employee.
- E. Action of an ERISA Plan in litigation: With an ERISA Plan in place, claims for benefits, including claims for wrongful denial of insurance benefits, may be tried in federal court, not in state court. A jury trial is usually not available, federal judges are usually more objective, and Plaintiff's attorneys usually have less experience and are less comfortable in the federal court system.
- F. Fraudulent claims: With a proper written Plan, the employer can make the employee prove that the employer was "arbitrary and capricious" in denying Plan benefits. This helps the employer control fraudulent benefit claims. A written Plan can clarify the employer's right to terminate the Plan and the employment of any employee. Unwritten injury benefit programs have been interpreted by Courts as providing employees an implied contractual right to continued employment.
- G. Plan offset against a workplace negligence claim: Workplace injury benefits paid by an AD&D policy under the Plan can be offset against a negligence claim arising from that incident.

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(A) A large manufacturing company was sued by an employee who fractured his elbow. The employee had engaged in "horseplay" and used a water hose to "wet down" a fellow employee who was seated in a rest room stall. As he ran from the area, the Plaintiff slipped, fell on his elbow and incurred a compound fracture. The client terminated the employee for "horseplay" and paid nothing other than the initial emergency first aid treatment. Following the first deposition, the Plaintiff agree to dismiss the case with the client paying two (2) weeks of severance pay. No medical or other payments were made.

(B) A mid-sized packaging company was sued by an employee who was scalped from the nape of his neck to his eyebrow. The employee had removed his hair net, a violation of a strict dress code policy and crawled beneath an operating sorting machine. His long hair was caught in the machine's pulley system resulting in his injury. As a result of the policy violation leading to the injury, the client terminated the employee for "violation of safety policy" and paid nothing other than the initial emergency first aid treatment. Litigation was filed for \$1.5 million. Following the first deposition, Plaintiff's counsel's \$500,000 settlement offer was refused. Following the second deposition, Plaintiff's counsel's \$150,000 settlement offer was refused. Approximately eighteen (18) months after litigation was filed, the case settled jointly between the machine manufacturer and the client. The client's settlement amount was minimal. (Due to the confidentiality agreement of the settlement, the exact amount cannot be revealed.)

The settlement in this case was not a result of a potential negligence exposure, but the result of an agreement between the client and the manufacture of the involved machine to remove all parties from the case, each Defendant sharing in the settlement dollar paid. They had chosen a "window of opportunity" to economically conclude the case.

In each of the above cases, no Attorney's fees were incurred by the clients, since ongoing legal services, from initial inquiry by Plaintiff's counsel, through discovery, until the time of trial, are included as a portion of the ongoing fee structure. This ongoing commitment to clients is the fundamental basis for their success as non-subscribers to workers' compensation in Texas and South Carolina.

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ASHMORE & RABON
ATTORNEYS AT LAW
ONE NINE EIGHT SEVEN SOUTH
GREENVILLE, SOUTH CAROLINA 29601
(803) 271-2394

A. J. RABON, JR.
A. J. RABON, JR.

B. O. Neil Rabon, Jr.

March 24, 1992

A. J. RABON, JR.
GREENVILLE, SC 29601
(803) 271-2394

(803) 271-2394

Paul A. Maxper, President
S. C. Financial Alternatives, Inc.
P.O. Box 231173
Montgomery, AL 36123

RE: Application of AYA Program to South Carolina Law

Dear Mr. Maxper:

You have recently requested that this office render an opinion as to the legal viability of the S.C. Financial Alternatives Employer/Employee Program in South Carolina. More specifically, you have asked that we review Texas law as it applied to the Employer/Employee Program of American Financial Alternatives, Inc., and to compare same to South Carolina law, seeking to determine what the differences are, if any, and the effect of these differences in the implementation of the Employer/Employee Program in this state.

In preparing this opinion, we have reviewed the AYA Employer/Employee Program, as well as both Texas and South Carolina Workers' Compensation Statutes. We have also reviewed various case law related to those statutes. We have reviewed the general tort law of each state and the general employer law of both states. We have not reviewed every case, and are not, of course, able to definitively anticipate what direction the South Carolina Courts will go in the various tort areas in the future, and our opinions in this regard are limited to the materials that we have reviewed and to the viability of this Program in South Carolina under the present Workmen's Compensation Statute and present case and statutory laws. Moreover, this opinion does not present a case by case analysis, but rather an overview in fairly general terms.

It is also appropriate, I think, to point out that both myself and my partner have a minority equity interest in S.C. Financial Alternatives, Inc. We will be serving as general counsel, as well as litigation counsel, and thus, we have a much heavier burden to carry in terms of our representations in this letter.

Both Texas and South Carolina statutes allow for the rejection of or non-subscription to, the workmen's compensation program of

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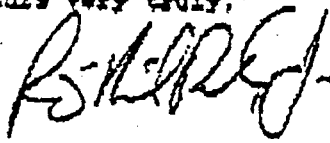
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Paul A. Harper, President
March 14, 1992
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implementing this non-subscriber approach as a practical matter
much longer than South Carolina.

With kind regards, I remain,

--- Yours very truly,



R. O'Neil Rabon, Jr.
Ashmore & Rabon
S.C.P.A., Inc. General Counsel

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Palmetto Hospital Trust

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each respective state. When employers choose this option, both states, by statute, require the employee to prove negligence on the part of the employer in order to recover for any losses the employee might have suffered as a result of an injury on the job. The employer, by statute, loses certain common law tort defenses normally available; namely, assumption of the risks, contributory negligence, and negligence of co-employees.

As to the right to be a non-subscriber, there is, for all practical purposes, no difference between South Carolina and Texas. Although there is substantially more case law related to this option in Texas, the South Carolina Courts have long recognized that an employer has the right to reject the act. Moreover, the Courts have clearly said that if an employer exercises that right, it was not the intent of the South Carolina Legislature to create a statutory right of recovery. "This statute purports only to deprive the non-assenting employer of certain named defenses, and it was not the intention of the Legislature, in addition to abrogating those defenses, to establish a statutory right of recovery based only on the fact that the employee sustained injuries 'by accidents arising out of or in the course of his employment.'" *Muckells vs Great Atlantic & Pacific Tea Company* (1939, 192 S.C. 156, 5 SC 2nd 841).

Once the election is made, Texas employers must operate under various reporting requirements under statutes relating to non-subscription. There are no such requirements in place in South Carolina that we have been able to determine, although one might reasonably expect that some reporting measures may be required in the future if a substantial number of employers begin to choose the option of non-subscription.

Both Texas and South Carolina operate under a comparative negligence approach within the tort recovery system. This approach to tort injuries seeks to distribute responsibility for damages more effectively and efficiently than the old contributory negligence standard. Previously, if a Plaintiff in the tort action was found to be negligent in a manner which contributed to his injury, he was completely barred from any recovery, regardless of the degree of his contribution to that injury. Adoption of the comparative negligence approach in Texas was made by the Texas Legislature, and Plaintiffs who contribute to their own injury are not completely and automatically barred from recovery. In instances when the contribution of negligence by a Plaintiff is equal to or less than the negligence of a named Defendant, the Plaintiff may enjoy a recovery, less the percentage reduced by the percentage of the negligence he contributed.

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EXHIBIT 7

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HB 504

Benedict

AN OVERVIEW OF ISSUES AND OPTIONS ON THE APPLICATION OF A 1% PAYROLL TAX ON EMPLOYERS AND EMPLOYEES

APRIL 1992

Prepared by



Montana Legislative Council

Montana Legislative Council
State Capitol, Room 138
Helena, Montana 59620
(406) 444-3064
FAX: (406) 444-3036

AN OVERVIEW OF ISSUES AND OPTIONS
ON THE APPLICATION OF A 1% PAYROLL TAX
ON EMPLOYERS AND EMPLOYEES

Prepared by

David D. Bohyer, Research Director
Montana Legislative Council

April 16, 1992

BACKGROUND AND INTRODUCTION

During the past 10 years, an "unfunded liability"* within Montana's workers' compensation system has grown to between \$360 million and \$433 million. The unfunded liability, isolated in the "old fund", has been the focus of several legislative committees and other groups, each of which has grappled with alternatives for eliminating the liability -- to this point, without success.

At the March 18, 1992, meeting of the Joint Select Committee on Workers' Compensation (hereinafter, Committee), a recommendation was tentatively adopted to increase the current 0.28% payroll tax on employers¹ to a full 1% of payroll and to impose the tax at a rate of 1% on employees as well. The Committee discussion also emphasized that the tax should be applied to a broad base as opposed to a narrow base.

In considering the expansion and extension of the payroll tax, the Committee also discussed mitigating the impacts of the tax on "low-income" employees and on "small businesses". The purposes of this paper are twofold: (1) to examine some of the direct and indirect impacts of the recommendation; and (2) to refine and clarify the recommendation for the purpose of developing appropriate legislation. The first purpose is addressed through the narrative in Part 1. The second purpose is fulfilled in Part 2 with an "issues and options checklist" -- a tool that can be used to logically proceed through several policy questions that must be answered for staff to draft legislation reflecting the Committee's wishes.

* The liability is caused by estimated outstanding claims and the costs of administering and managing the claims, benefits, and so forth. The reason that the liability is unfunded is that there is no income to pay for the costs, nor are there any assets.

PART 1
AN OVERVIEW OF A 1% PAYROLL TAX

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THE COMMITTEE'S TENTATIVE RECOMMENDATION

The substance of the Committee's recommendation was to begin drafting legislation that would impose a 1% payroll tax on employers and employees for the express purpose of paying off the unfunded liability of the "old fund".² Discussion accompanying the motion included the possibility and advisability of mitigating the impact of the tax on "low-income" employees and on "small businesses". Diverting the receipts from the unemployment insurance administration account³ was also discussed as another means of reducing the impact on employers.

A primary purpose of setting the payroll tax at the 1% level and imposing the tax on employees as well as on employers was to eliminate the unfunded liability in a short time, approximately 5 years. While bonding was discussed as an option, it was rejected because of a consensus that the state is extensively bonded currently, that bonding could cost more in the long run than paying off the unfunded liability debt with ready cash flow,* and that the liability would continue for several more years.

HOW THE PAYROLL TAX COULD WORK

Section 39-71-2503, MCA, imposes a tax at the rate of 0.28% on the payroll of every employer for employments covered under 39-71-401, MCA. The basis for determining payroll is wages paid, as defined in 39-71-123, MCA. Payroll tax payments are to be made to the Department of Revenue quarterly. **

* An alternate school of thought suggests that as financing rates are currently very low for state bonding and return rates are relatively high, the state would actually gain an advantage if it sold bonds to amortize the unfunded liability. As long as investment earnings generate higher returns than the financing of bonds costs, the state would stand to gain.

** Employers whose withholding of individual income taxes exceeded \$300,000 for the preceding calendar year are required to make payroll tax payments weekly. See 15-30-204(2), MCA.

To implement the Committee's recommendation, Montana statutes would have to be: (1) amended to reflect the 1% rate on employers; and (2) enacted to impose the 1% tax on employees.

For employers, 39-71-2503, MCA, could be amended simply by changing the tax rate from 0.28% of payroll to a full 1% of payroll. For employees, language similar to language in Senate Bill No. 405 from the 51st Legislative Session (1989) could be enacted.

HOW EMPLOYERS AND EMPLOYEES MIGHT BE AFFECTED

The imposition of a 1% payroll tax on employers and employees would be a significant tax increase, especially on the base that is, in large part, income. Imposed on employers and employees, the 1% payroll tax would generate about \$100 million annually.*

In its first year of implementation, the 0.28% tax on employers generated about \$12.765 million, indicating a payroll base of about \$4.58 billion.⁴ Recent research indicates that a more current (1990) base is about \$4.996 billion.⁵ Using the \$4.996 billion figure as a base, a 1% tax would generate about \$49.96 million annually from employers. Because the payroll base is the same for employees, a like amount of \$49.96 million in payroll tax revenue would derive from employees.

EFFECT ON SMALL BUSINESS

In order to estimate the effect of the tax on small business employers, the Committee and the Legislature must more clearly define "small business". In many cases, businesses with fewer than 100 employees are classified as

* To put into some context the magnitude of \$100 million annually in Montana's state revenue scheme, House Joint Resolution No. 1, (Special Laws of January 1992), estimates corporation license tax collections for FY 1992 and FY 1993, respectively, at about \$53.3 million and \$61 million. Similarly, total individual income tax collections for FY 1992 and FY 1993, respectively, are estimated at about \$317 million and \$324 million.

small businesses.⁶ In Montana, however, an employer of 99 employees would generally be considered something other than a small business. Table 1 illustrates a breakdown of Montana businesses by the average monthly number of employees and by average monthly wages per employee.

TABLE 1 DISPERSION OF MONTANA BUSINESSES BY NUMBER OF EMPLOYEES AND AVERAGE MONTHLY WAGES			
Size of Firm by No. of Employees	Average No. of Firms Reporting	Average Monthly Employment*	Average Mon. Wages per Employee
0	3,934	900	\$1,204
1 - 4	13,149	28,064	1,217
5 - 9	4,924	32,035	1,260
10 - 19	2,792	36,950	1,335
20 - 49	1,842	55,399	1,404
50 - 99	576	39,235	1,453
100 - 249	261	37,920	1,618
250 - 499	66	22,509	1,871
500 - 999	20	13,267	2,389
1,000 +	7	11,182	1,781
TOTAL or AVERAGE	27,571	276,241	\$1,496

Source: Montana Department of Labor and Industry, Research, Training & Safety Division; and Montana Legislative Council.

Alternative indicators of a business being a small business might include annual payroll, annual gross sales, or annual net or taxable income (for corporation license tax purposes). Table 2 illustrates the dispersion of Montana corporations, using Montana corporate taxable income as the measure.

Finally, precautions should be taken to ensure that any mechanism for mitigating the impact of the payroll tax is effectively and efficiently targeted to provide the intended benefit at the intended individual enterprise level.

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TABLE 2			
DISPERSION OF MONTANA CORPORATIONS BY NET INCOME (1990)			
MONTANA TAXABLE INCOME BRACKET	NUMBER OF CORPORATIONS	PERCENTAGE OF CORPORATIONS	CUMULATIVE PERCENTAGE
< \$0	4,618	29.8%	29.8%
= \$0	4,137	26.7%	56.5%
\$1-\$1,000	1,142	7.4%	63.8%
\$1,001-\$4,000	969	6.2%	70.1%
\$4,001-\$16,000	1,580	10.2%	80.3%
\$16,001-\$48,000	1,548	10.0%	90.2%
\$48,001-\$1,000,000	1,389	9.0%	99.2%
\$1,000,000 or more	125	0.8%	100.0%
TOTAL	15,508	100.1%*	100.0%

Source: Montana Department of Revenue, Office of Information and Research

* Due to rounding.

POSSIBLE EFFECTS ON "LOW-INCOME" EMPLOYEES

Determining how a 1% payroll tax might affect low-income employees is difficult until the Committee and the Legislature more clearly define "low income". However, some review of Montana individual income should be informative and instructive. Statistics for Montana from the 1990 census⁷ show the following:

- For households, families, and nonfamily households, the median incomes in 1979 and 1989 were:

	<u>1979</u>	<u>1989</u>
* Households:	\$15,420	\$22,988
* Families:	\$18,413	\$28,044
* Nonfamily households	NA	\$12,502

- Montana per capita income in 1989 was \$11,213 compared to a 1979 per capita income of \$6,589. (National 1989 and 1980 per capita income, respectively, were \$17,596 and \$9,919 -- *Statistical Abstract of the United States*, 1991, Bureau of the Census.)
- For 1989 Montana households, average (mean) wage and salary income was \$25,575.

Additionally, the 1990 census showed the dispersion of households across an income spectrum. The information is illustrated in Table 3.

TABLE 3	
DISPERSION OF MONTANA INCOME BY NUMBER OF HOUSEHOLDS: 1989	
Income in 1989	Number of Households
Less than \$5,000	22,480
\$5,000 to \$9,999	38,514
\$10,000 to \$14,999	37,554
\$15,000 to \$24,999	66,766
\$25,000 to \$34,999	52,485
\$35,000 to \$49,999	48,894
\$50,000 to \$74,999	28,198
\$75,000 to \$99,999	6,803
\$100,000 to \$149,999	3,390
\$150,000 or more	1,835
Total number of households	306,919
Median household income	\$ 22,988

Source: STF3A, U.S. Bureau of the Census, 1991.

Other statistics compiled from the 1990 census show the following for Montana:

- Median household income for the state fell from \$25,844 in 1979 to \$22,988 in 1989, a decrease of 11.1 percent, after adjusting for the increase in consumer prices.
- Real per capita income rose from \$11,043 in 1979 to \$11,213 in 1989, an increase of 1.5 percent.

- The poverty rate for persons went up from 12.3 percent in 1979 to 16.1 percent in 1989, while the number of persons in poverty rose from 94,280 in 1979 to 124,853 in 1989.
- The poverty rate for related children under 18 years was 19.9 percent in 1989, while the poverty rate for persons 65 and over was 12.5 percent.
- The poverty rate for families went up to 12.0 percent in 1989 from 9.2 percent in 1979, while the number of families in poverty rose from 19,019 in 1979 to 25,691 in 1989.
- The poverty rate for families with a female householder and no spouse present was 39.7 percent in 1989.

Individuals and Montana's Personal Income Tax

In Montana, people's incomes are subject to an individual income tax under Title 15, chapter 30, MCA. The nominal rates of tax applicable to taxable income are stated in 15-30-103, MCA, and appear in column 3 of Table 4. The information in column 2 of Table 4 shows the amounts of taxable income for tax year 1991, indexed for inflation.

Table 4 suggests that Montana has a fairly progressive individual income tax up to \$57,601 (indexed for 1991) with nominal rates beginning at 2% and "graduating" to a top marginal rate of 11%. However, Montana does not tax "gross" income, but allows a number of adjustments to income, including deductions, exemptions, exclusions, credits, deferrals, and so forth. The adjustments shelter some types of income from taxation, which has the effect of mitigating the progressivity of the tax as represented nominally. In short, after adjustments, the average "effective" tax rate for Montana residents is 3.09% and the average effective tax rate for householders receiving more than \$150,00 annually is 5.72%.⁸

TABLE 4		
MONTANA 1991 TAXABLE INCOME BRACKETS INDEXED FOR INFLATION		
Nominal Taxable Income (\$)	1991 Indexed Taxable Income (\$)	Nominal Income Tax Rates
0-1,000	0-1,600	2%
1,001-2,000	1,601-3,300	3%
2,001-4,000	3,301-6,600	4%
4,001-6,000	6,601-9,900	5%
6,001-8,000	9,901-13,200	6%
8,001-10,000	13,201-16,400	7%
10,001-14,000	16,401-23,000	8%
14,001-20,000	23,001-32,900	9%
20,001-35,000	32,901-57,600	10%
35,001 +	57,601 +	11%

Source: Montana Department of Revenue; also "Analysis of the Montana Personal Income Tax Structure" by Jeff Martin, Montana Legislative Council, March 1992, Table 6, p. 15.

Income Taxes and Payroll Taxes Compared

Table 5 illustrates a distribution of personal income tax burden for Montana residents by expanded income group for tax (calendar) year 1990.*

Expanded income is used as the measure rather than an adjusted income because the relationship of taxes paid to expanded income measure more accurately describes effective rates.

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* Expanded income is a measure of income that includes all income reported for tax purposes, before adjusting for deductions or exemptions.

TABLE 5						
DISTRIBUTION OF PERSONAL INCOME TAX BURDEN FOR MONTANA RESIDENTS BY EXPANDED INCOME GROUP, 1990						
Expanded Income Bracket (Thousands of dollars)	Number of Households	Expanded Income (Thousands of dollars)	Taxes Paid (Thousands of dollars)	Cumulative Income Share	Cumulative Share of Taxes Paid	Effective Tax Rate
0	4,650	0	0	0.0%	0.0%	0.0%
0-6	61,200	183,101	1,095	2.3%	0.4%	0.60%
6-8	19,050	132,745	1,242	4.0%	1.0%	0.94%
8-10	16,050	143,397	1,723	5.8%	1.7%	1.20%
10-12	17,574	193,448	2,241	8.2%	2.6%	1.16%
12-16	29,829	415,646	6,772	13.5%	5.3%	1.63%
16-20	24,270	437,515	7,678	19.0%	8.5%	1.76%
20-25	25,896	580,940	12,525	26.3%	13.6%	2.16%
25-30	21,576	589,834	14,533	33.7%	19.5%	2.46%
30-40	36,609	1,274,746	36,193	49.8%	34.2%	2.84%
40-50	24,492	1,095,283	34,488	63.6%	48.3%	3.15%
50-70	21,211	1,222,101	44,004	78.9%	66.2%	3.60%
70-100	7,152	583,912	23,858	86.3%	75.9%	4.09%
100-150	2,865	343,943	16,543	90.6%	82.7%	4.81%
150 +	2,251	744,194	42,551	100.0%	100.0%	5.72%
Total	314,675	7,940,805	245,447	NA	NA	3.09%

Note: Totals may not add due to rounding.

Source: Montana Department of Revenue; also "Analysis of the Montana Personal Income Tax Structure", Jeff Martin, Montana Legislative Council, March 1992, Table 6, p. 15.

Relationship of Income Taxes and the 1% Payroll Tax

It is clear that the tax base for the payroll tax ("wages") is significantly different than the tax base for the individual income tax. For 1992, for example, total Montana wages and salaries are estimated at \$6.229 billion and Montana personal income is estimated at \$12.969 billion.⁹ Analysis of the respective bases and of taxes paid or payable suggests several patterns:

- Average effective income tax rates on Montana resident's income are progressive to higher levels of income (at least \$150,000), then proportionate.
- Wages as a proportion of total income are consistent between the lower and upper income groups.¹⁰
- Average effective payroll tax rates, if imposed at a flat 1 % of wages, would be regressive.

The progressivity of effective income tax rates is illustrated in Table 5, and the proportionality of wages across the income spectrum is evidenced in analysis done by Jim Standaert, Office of the Legislative Fiscal Analyst. Finally, data on income, payroll, and tax rates are shown in Tables 6 and 7.

TABLE 6				
WAGE AND SALARY DATA BY INCOME DECILE GROUP				
Decile Group	Household Income Range	Average Wages and Salaries	Total Wages and Salaries	As a Percent of Total
1	\$ <0 - \$2,953	1,394	49,983,750	1.0
2	\$2,953 - \$6,085	3,023	93,875,400	1.9
3	\$6,085 - \$9,590	4,661	148,217,700	3.0
4	\$9,590 - \$13,238	7,182	214,781,742	4.3
5	\$13,238 - \$17,956	9,793	303,606,522	6.1
6	\$17,956 - \$23,484	13,721	429,862,503	8.6
7	\$23,484 - \$30,404	18,191	564,551,268	11.3
8	\$30,404 - \$38,822	25,829	800,818,827	16.0
9	\$38,822 - \$51,432	32,536	1,008,595,021	20.2
10	\$51,432 +	45,017	1,381,929,398	27.7
	TOTAL	NA	4,996,222,142	100.1*

Source: Jim Standaert, Associate Fiscal Analyst, Office of the Legislative Fiscal Analyst.

* Due to rounding.

The information in Table 7 is telling in several ways. First, the figures in column 5 show that, as a percentage of income tax liability, estimated payroll tax liability is significantly higher for lower-income employees than for higher-income employees, i.e., it is regressive. Second, the information in column 4 shows that, regressive as the payroll tax is, the actual, nominal dollars of payroll tax paid on the average is a fairly modest amount, ranging from an average of \$14 annually (\$0.27 weekly) in the lowest decile group to an average of \$450 annually (\$8.65 weekly) in the highest decile group.

TABLE 7				
INCOME AND 1% PAYROLL TAX LIABILITY BY INCOME DECILE GROUP				
Decile Group	Household Income Range	Average Income Tax Liability	Average Payroll Tax Liability	Payroll Tax as a Percent of Income Tax
1	\$ <0 - \$2,953	\$ 7	\$ 14	211%
2	\$2,953 - \$6,085	34	30	90%
3	\$6,085 - \$9,590	81	47	58%
4	\$9,590 - \$13,238	152	72	47%
5	\$13,238 - \$17,956	258	98	38%
6	\$17,956 - \$23,484	417	137	33%
7	\$23,484 - \$30,404	630	182	29%
8	\$30,404 - \$38,822	965	258	27%
9	\$38,822 - \$51,432	1,403	325	23%
10	\$51,432 +	3,858	450	12%
	TOTAL/ AVERAGE	\$ 765	\$ 159	21%

Source: Letter to Select Committee on Workers' Compensation from Jim Standaert, Office of the Legislative Fiscal Analyst, April 6, 1992.

As is the case with mitigation measures for "small businesses", the mechanism(s) adopted to mitigate the impact of the payroll tax must be carefully conceived and articulated to ensure that the benefits accrue to the intended persons.

REVENUE MAINTENANCE AND CONSIDERATIONS

If any mechanisms are adopted to mitigate the impact of payroll taxes on low-income wage earners and small businesses, revenue to some fund or funds will be reduced below those estimated initially. For example, if the Committee and the Legislature determine that persons earning the hourly minimum wage should be exempt from the payroll tax, revenue collected from the tax would be less than the amount initially anticipated (when imposed on all payroll).

Similarly, if a deduction or credit is adopted as the mitigation mechanism, payroll tax revenue would be maintained but individual income tax revenue and corporation license tax revenue would be reduced, thereby reducing allocations to the state's general fund, school equalization account, and long-range building program funds.

Consequently, in order to maintain estimated revenues to retire the unfunded liability and to maintain other state revenue funds and accounts, mitigation will have to be offset through higher payroll taxes on those who are subject to the tax, the term for retiring the liability will have to be revised, or some other revenue source will have to be increased to offset the loss.

SUMMARY AND CONCLUSIONS

The unfunded liability in the "old fund" of Montana's workers' compensation system has been growing steadily for the past decade. Previous attempts to solve the problem have not resulted in eliminating the liability.

The Joint Select Committee on Workers' Compensation has tentatively recommended that the payroll tax currently imposed on employers be increased from 0.28% of payroll to a full 1% of payroll and that the tax also be imposed at a full 1% on employees' wages. If the recommendation is implemented, it is estimated that the unfunded liability could be eliminated in as little as 5 years.

The Committee's concerns with mitigating the impacts of the payroll tax on "small business employers" and on "low-income" employees must be clarified so that appropriate legislation may be drafted. Specifically, the Committee and the Legislature will have to clearly define a "small business" and a "low-income" employee.

A payroll tax of 1% would exact a moderate, nominal amount of tax on an individual basis. For wage earners in the lowest income decile, the average payroll tax would be about \$14 annually or \$0.27 per week; at the highest income decile, the average payroll tax would be about \$450 annually or \$8.65 per week. An alternative illustration might be that a person earning \$200 per week (\$10,400 annually) would pay about \$2 per week in payroll taxes (or \$104 per year), while a person earning \$1,000 per week (\$52,000 annually) would pay about \$10 per week in payroll taxes (or \$520 annually).

Even at the modest, nominal level of payroll tax, the tax itself is regressive. For wage earners in the lowest income decile, average payroll taxes paid exceed 200% of average income taxes paid. For wage earners in the middle income deciles, payroll taxes would be about 35% of income taxes paid, and for wage earners in the highest income decile, payroll taxes would be about 12% of income taxes paid. Overall, based on 1990 data for Montana residents, estimated payroll tax liability of about \$50 million on employees is equivalent to a surtax of about 21% on total Montana resident income tax liability of about \$250 million.

If the impact of the payroll tax is to be mitigated for low-income employees and for small business employers, some mechanism will have to be effected to maintain revenue levels. Additionally, the mechanism chosen to provide mitigation will have to be carefully crafted to ensure that intended benefits and goals are being achieved.

The option tentatively recommended by the Committee, i.e., a full 1% payroll tax on both employers and employees, should achieve the

Committee's goal of retiring the unfunded liability in as little as 5 years using current cash flow.

Finally, in order that appropriate legislation can be drafted to reflect the Committee's recommendation, further clarification of terms must be done.

The "issues and options" worksheets in Part 2 of this paper are provided to assist the Committee in its work.

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PART 2
ISSUES AND OPTIONS WORKSHEETS

The following worksheets list several options for each of several issues that must be addressed for appropriate, clearly articulated legislation to be drafted in order to reflect the Committee's tentative recommendation.

Neither the issues nor the options identified are all-inclusive, but they are provided to the Committee as a starting point and discussion tool. Similarly, the order in which the issues and options are presented does not indicate a priority or a preference.

For the convenience of the Committee's members, each issue is presented in a self-contained format on a separate page. Each issue is accompanied by options and preliminary discussion.

ISSUE 1: SHOULD THE IMPACT OF THE 1% PAYROLL TAX ON
EMPLOYEES BE MITIGATED FOR "LOW-INCOME" EMPLOYEES?

___ Yes ___ No

DISCUSSION

The issue of mitigating the impacts of the payroll tax on low-income employees arises for perhaps several reasons, among which is the philosophical and economic principle of taxes being imposed based on a taxpayer's "ability to pay". As the base for the payroll tax is, for wage earners, arguably, a similar base upon which individual income taxes are imposed, the Montana individual income tax provides a reasonable comparison.

Reports prepared by the staff of the Montana Legislative Council* and the Montana Department of Revenue** indicate that Montana currently adheres to a moderately progressive income tax structure. Those persons at the lowest end of the income spectrum, i.e., less than \$6,000 per year, pay an effective tax rate of 0.6%. Those persons at the middle of the income spectrum, i.e., between \$20,000 and \$25,000 per year, pay an effective tax rate of 2.16%. Those persons at the highest end of the income spectrum, i.e., those persons with income in excess of \$150,000 per year, pay an effective tax rate of 5.72%.***

A payroll tax at 1% of wages would be nominally proportional on each dollar of wages earned. However, the effective rate on a broader measure of income would show that a flat 1% payroll tax would be regressive -- the payroll tax would take a larger share of income of low-income employees compared to moderate or higher income persons.

If a like amount of revenue were to be generated from sources other than payroll, e.g., Montana adjusted gross income, nominal and effective rates could potentially be lowered or, in the alternative, the liability could be paid off more quickly.

* See "Analysis of the Montana Personal Income Tax Structure" by Jeff Martin, Montana Legislative Council, March 1992.

** Memorandum TO: Revenue Oversight Committee, SUBJECT: Individual Income Tax Liability by Taxpayer Income Class, FROM: Denis Adams, Director, Montana Department of Revenue, March 19, 1992.

*** Martin, Table 6, p. 15.

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ISSUE 2: WHAT CRITERION SHOULD BE ESTABLISHED FOR DETERMINING THE "LOW-INCOME" STATUS OF AN EMPLOYEE?

- OPTIONS: A. ____ \$X or less per hour of wages
- B. ____ \$Y or less per year of total wages
- C. ____ \$Z or less per year of total household income
- D. ____ other criterion _____

DISCUSSION

If it is determined by the Legislature that the impact of the payroll tax should be mitigated for "low-income" employees, the Legislature will also have to define what measure(s) must be used to determine "low-income".

In making a "low-income" determination, the Legislature may wish to use an hourly wage as the basis. Hourly wages that could be used to signify low-income status might include the following:

- federal minimum wage
- state minimum wage (39-3-409, MCA)
- mean (average) hourly wage for Montana
- median hourly wage for Montana.

If the Legislature determines that the basis of determination should be annual wages, measures that could be used to signify low-income status might include the following:

- annualized federal minimum wage
- annualized state minimum wage (39-3-409, MCA)
- mean (average) annual wage for Montana
- median annual wage for Montana.

For these measures, the Legislature must determine whether the measure is to be applied to the individual only, the individual's family, or the individual's household. The Legislature must also determine if gross income is the appropriate basis, or if an adjusted measure is the appropriate basis, e.g., federal adjusted gross income or federal taxable income or Montana adjusted gross income or Montana taxable income.

Administrative problems are another matter altogether.

ISSUE 3: WHAT MECHANISM SHOULD BE IMPLEMENTED TO MITIGATE THE IMPACT OF THE 1% PAYROLL TAX ON "LOW-INCOME" EMPLOYEES?

- OPTIONS: A. ☐ For individual income tax purposes, allow a deduction equal to the amount of payroll tax paid by the employee.
- B. ☐ For individual income tax purposes, allow a credit equal to the amount of payroll tax paid by the employee.
- C. ☐ For individual income tax purposes, allow a refundable credit equal to the amount of payroll tax paid by the employee.
- D. ☐ For an individual classified as "low income", do not impose the payroll tax on wages.
- E. ☐ Other mechanism _____

DISCUSSION

The mechanism for mitigation is very important if mitigation is actually to occur for low-income employees. For example, for tax year 1990, about 43% of Montana income tax returns claimed the standard deduction. Consequently, if an income tax deduction is adopted, approximately 43% of filers would not be able to claim a deduction for payroll taxes paid.

If a tax credit is adopted, it would have to be crafted very carefully to ensure that only truly low-income employees could take advantage of it. All adjustments to income would have to be carefully reviewed and analyzed. Additionally, a credit could have a larger impact -- as compared to a deduction -- on other revenue funds.

If a version of the option of not imposing the tax on low-income employees is adopted, a clear definition of "low income" will have to be established in advance.

Again, administrative complications are another matter.

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ISSUE 4: SHOULD THE IMPACT OF THE 1% PAYROLL TAX BE
MITIGATED FOR "SMALL BUSINESSES"?

___ Yes ___ No

DISCUSSION

Whether or not mitigation of the impact of the payroll tax is recommended for small business employers, the politics of determining "small businesses" may be as difficult as the practical application of the mitigation mechanism.

Such terms as "fairness", "ability to pay", "low-margin business", "chilling effects", "bad business climate" and others might be invoked in a discussion of mitigation. Regardless of the measure(s) chosen to distinguish a "small business" from other businesses, arguments will likely abound (and perhaps legitimately so) that the measure should be either marginally raised or lowered. Well-reasoned and convincing arguments will have to be developed by the Committee to assuage the feelings of businesses that do not meet the small business definition and, therefore, must pay the 1% tax.

ISSUE 5: WHAT CRITERIA SHOULD BE ESTABLISHED FOR DETERMINING THE "SMALL BUSINESS" STATUS OF A BUSINESS?

- OPTIONS: A. ☐ X employees or fewer
- B. ☐ Y payroll or less per year
- C. ☐ \$Z or less per year of gross income
- D. ☐ \$N or less per year of net income
- E. ☐ Other criterion _____

DISCUSSION

Determining the identity of "small businesses" will be very difficult to establish and defend. Practically speaking, whatever criteria are adopted will exclude some employers that view themselves as small businesses, thus subjecting them to the tax.

Politically speaking, developing a credible, defensible rationale for making a distinction at whatever level is recommended by the Committee and the Legislature will be difficult but must be done for appropriate legislation to be drafted by staff.

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ISSUE 6: WHAT MECHANISM SHOULD BE IMPLEMENTED TO MITIGATE THE IMPACT OF THE 1% PAYROLL TAX ON "SMALL BUSINESSES"?

- OPTIONS:**
- A. ☐ For corporation license tax or income tax purposes, allow a deduction equal to the amount of payroll tax paid by the small business employer.
 - B. ☐ For corporation license or income tax purposes, allow a credit equal to the amount of payroll tax paid by the small business employer.
 - C. ☐ For corporation license or income tax purposes, allow a refundable credit equal to the amount of payroll tax paid by the small business employer.
 - D. ☐ For a business classified as a "small business", do not impose the payroll tax on wages.
 - E. ☐ Other mechanism _____

DISCUSSION

The issues involved in identifying an appropriate mitigating mechanism for small businesses are essentially parallel to those involved for mitigation for low-income employees. The key is to ensure that the mechanism effectively mitigates the impact for the intended small business employers.

ISSUE 7: WHAT MECHANISMS, IF ANY, SHOULD BE ADOPTED TO RECOUP LOST REVENUE FROM THE MITIGATION PROVIDED TO LOW-INCOME EMPLOYEES AND TO SMALL BUSINESSES?

- OPTIONS: A. ☐ Increase the payroll tax rate to offset the revenue lost from exempt employees and businesses.
- B. ☐ Recommend a general fund appropriation to offset the revenue lost from exempt employees and businesses.
- C. ☐ Raise individual income tax rates or corporation license tax rates to offset the tax revenue lost to deductions or credits due eligible employees and businesses.
- D. ☐ Impose a surtax on individual income taxes and on corporation license taxes to offset the tax revenue lost to deductions due eligible employees and businesses.
- E. ☐ Other mechanism _____

DISCUSSION

Any mechanism for mitigating the impact of the payroll tax will have the effect of reducing revenue to one or more state revenue funds. If low-income employees or others are eligible to deduct the amount of payroll tax paid on their Montana individual income tax return, then revenue accruing to the state general fund, school equalization account, and long-range building fund could each be reduced. A larger negative effect would accrue from an income tax credit of an equal amount.

Similarly, if small businesses are eligible to deduct the amount of payroll tax paid on their Montana corporation license tax return, the state general fund, school equalization account, and long-range building fund could each be reduced. Again, the same effect would accrue from a tax credit.

If some employees or businesses are categorically exempted from the payroll tax, revenues expected from the tax (when imposed on all payroll) would not be generated. To offset the impact, the payroll tax rate would have to be increased for those subject to the tax to generate a like amount of estimated revenue, i.e., about \$50 million.

NOTES

1. See 39-71-2503, MCA.
2. See "Minutes of the Joint Select Committee on Workers' Compensation", March 18, 1992, prepared by Montana Legislative Council.
3. See 39-51-406, MCA. The code section describes the account, the purposes of the account, and sources of revenue.
4. See "State Compensation Mutual Insurance Fund: Options for Remedial Actions to Deal with Problems of the "Old Fund"", by Paul E. Verdon, Montana Legislative Council, January 29, 1992, p.1. However, at the March 18, 1992, meeting of the Joint Select Committee on Workers' Compensation, Representative Benedict stated that Montana has "\$4,427,666,667 in covered payroll every year".
5. Letter to the Select Committee on Workers' Compensation, from Jim Standaert, Associate Fiscal Analyst, Office of the Legislative Fiscal Analyst, April 6, 1992. This information is based on data from Montana Department of Revenue files on the Montana individual income tax. The 1990 income figures suggest annual growth in payroll between 1987 and 1990 of about 2.9%.
6. For a relevant discussion on defining a "small business", see *The State of Small Business: A Report to the President*, U.S. Small Business Administration, 1990, pp. 8-12.
7. 1990 Census of Population and Housing: Summary Tape File 3A (STF3A), U.S. Bureau of the Census, March 1992.
8. "Analysis of the Montana Personal Income Tax Structure" by Jeff Martin, Montana Legislative Council, March 1992, Table 4, p. 12.
9. House Joint Resolution No. 1, Special Laws of January 1992, Montana Legislative Council, Helena, Montana.
10. Letter from Jim Standaert to the Joint Select Committee on Workers' Compensation, April 8, 1992.

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111-574

Excerpt

OFFICE OF THE LEGISLATIVE AUDITOR
SCHEDULE OF PROJECTED LIABILITY PAYMENTS AND CASH NEEDS

9348s1&1
03:10 PM
02/08/93

PAYROLL INFLATOR OF 5% USED
AS REQUESTED BY LEGISLATORS

THIS SPREADSHEET PREPARED WITH
THE FOLLOWING ASSUMPTIONS:

FISCAL YEAR	TOTAL PROJECTED		BOND		TOTAL		EMPLOYEE		EMPLOYER		PROJECTED		THE FOLLOWING ASSUMPTIONS:
	LIABILITY PAYMENTS		DEBT PAYMENTS		EXPENSE	PAYROLL TAX	PAYROLL TAX	PROJECTED END OF YEAR CASH	INTEREST EARNINGS	PAYROLL TAX OF-->			
											1994-98	1.0000%	
1994	\$51,269,234		\$11,319,361		\$62,588,595	\$53,818,565	\$53,818,565	\$44,854,166	\$1,255,869				
1995	\$43,147,042		\$11,318,181		\$54,465,223	\$56,509,493	\$56,509,493	\$104,795,758	\$2,917,830		COVERED PAYROLL-->	\$4,881,502,500	
1996	\$37,847,457		\$11,320,631		\$49,168,088	\$59,334,968	\$59,334,968	\$177,623,889	\$4,940,434		COST OF CAPITAL-->	5.5000%	
1997	\$33,959,999		\$11,317,544		\$45,277,543	\$62,301,716	\$62,301,716	\$262,547,857	\$7,301,008		PAYROLL INFLATION RATE-->	5.0000%	
1998	\$30,193,073		\$11,318,244		\$41,511,317	\$65,416,802	\$65,416,802	\$360,086,572	\$10,013,018		BEGINNING CASH BALANCE-->	(\$26,367,966)	
1999	\$121,053,761		\$142,439,836		\$263,493,597			\$71,301,581	\$2,971,975				
	\$317,470,567		\$199,033,797		\$516,504,363	\$297,381,545	\$297,381,545		\$29,400,135		THIS SPREADSHEET CALCULATED THE		
											FOLLOWING FINANCIAL RELATED DATA:		
											TOTAL EXPENSE	\$516,504,363	
											YEAR PAYROLL TAX ENDS	1999	

LOANS FROM NEW FUND	OTHER SOURCES
1993	\$26,367,966

\$29,400,135 THIS SPREADSHEET CALCULATED THE
 =====
 FOLLOWING FINANCIAL RELATED DATA:
 TOTAL EXPENSE \$516,504,363
 YEAR PAYROLL TAX ENDS 1999

DATE 2-10-93

SELECT WORKERS' COMP

~~SENATE~~ COMMITTEE ON H.B. 470, 445, 504

BILLS BEING HEARD TODAY: _____

Name	Representing	Bill No.	Check One	
			Support	Oppose
<i>James P. Demid</i>	<i>CWCSI</i>	<i>470</i>	<i>X</i>	
<i>Harlee Thompson</i>	<i>MBIA + CWCSI</i>	<i>HB 470</i>	<i>X</i>	
<i>Steve Manterville</i>	<i>MT Assoc Realtors</i>	<i>470</i>		
<i>Bill Grace</i>	<i>MBIA</i>	<i>470</i>	<i>✓</i>	
<i>Duane THOMAS</i>	<i>Carroll College</i>	<i>439</i>	<i>✓</i>	<i>✓</i>
<i>George Wood</i>	<i>MT Self Insurers Assn</i>	<i>456</i> <i>504</i>	<i>✓</i>	<i>✓</i>
<i>Wiley Johnson</i>	<i>NFIB</i>	<i>456</i> <i>504</i>	<i>✓</i>	<i>✓</i>
<i>Wiley Johnson</i>	<i>NFIB</i>	<i>470</i> <i>455</i>	<i>✓</i>	<i>✓</i>
<i>Charles R. Brooke</i>	<i>MT Rot. & L. Assoc</i>	<i>504</i>		<i>✓</i>
<i>Char Mahoney</i>	<i>DOR</i>	<i>504</i>		
<i>Dennis Burr</i>	<i>MT Tourist Assoc</i>	<i>504</i>		<i>✓</i>
<i>Russell B Hill</i>	<i>MTZA</i>	<i>HB 455</i>	<i>✓</i>	
<i>Mont. Bldg Industry Assoc</i>	<i>Nancy app</i>	<i>HB 470</i>	<i>✓</i>	
<i>Bob Olsen</i>	<i>MT Hospital Assn</i>	<i>el Amend</i> <i>504</i>		<i>✓</i>
<i>Don Judge</i>	<i>MT STATE AFL-CIO</i>	<i>HB 455</i> <i>HB 470</i>	<i>✓</i>	
<i>Don Judge</i>	<i>MT STATE AFL-CIO</i>	<i>HB 504</i>		<i>✓</i>

VISITOR REGISTER

PLEASE LEAVE PREPARED STATEMENT WITH COMMITTEE SECRETARY

DATE 2-10-93

~~SENATE~~ COMMITTEE ON SELECT WORKERS' COMPENSATION

BILLS BEING HEARD TODAY: 470 445 504

Name	Representing	Bill No.	Check One	
			Support	Oppose
John Malachuk	M.F. + M.F. + S.C.	504		X
Carl Schweitzer	Mont Aut Assoc	470	X	
MIKE MICONE	MTCA			504
Don Allen	RWCSI		470 ✓	
Steve Turkiewicz	MT Auto Dealers Assn	504		✓

VISITOR REGISTER

PLEASE LEAVE PREPARED STATEMENT WITH COMMITTEE SECRETARY