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Joint Committee on Finance

Paper #741

Increase Penalties for UI Fraud (DWD -- Unemployment Insurance)

[LFB 2015-17 Budget Summary: Page 558, #3]

CURRENT LAW

Under current law, a claimant who conceals work performed, wages earned, or another material fact concerning benefit eligibility when filing a weekly claim certification must repay the full amount of benefits for each week the individual provided inaccurate information. In addition, the claimant is ineligible for future benefits in amounts equivalent to two times the weekly benefit rate for the first act of concealment; four times the weekly benefit rate for the second act; and eight times the weekly benefit rate for each act subsequent to the second determination. This ineligibility is applied against benefits and weeks of eligibility for which the claimant would otherwise be eligible after the week of concealment. Furthermore, consistent with federal directives, DWD assesses a penalty against the claimant in an amount equal to 15 percent of the benefits erroneously paid to the claimant as a result of one or more acts of concealment.

Also, under current law, any person who knowingly makes a false statement or representation to obtain UI benefit payments, either for himself or herself or for any other person, may be fined not less than \$100 nor more than \$500 or imprisoned for not more than 90 days, or both.

GOVERNOR

This bill would increase, from 15 percent to 40 percent, the surcharge on certain fraudulent overpayments made to UI claimants.

The bill would also impose a set of graduated criminal penalties for a person who knowingly makes a false statement or representation to obtain UI benefit payments, either for

himself or herself or for any other person. The increased criminal penalties listed in Table 1 would mirror the existing penalties contained in the criminal statutes for theft under Wis. Stat. 943.20.

TABLE 1

Proposed Increase in Criminal Penalties

| <u>If the value of UI benefits obtained:</u> | <u>Guilty of:</u> | <u>Maximum criminal punishment</u> |
|--|---------------------|---|
| Does not exceed \$2,500 | Class A misdemeanor | Not to exceed \$10,000 or imprisonment not to exceed 9 months, or both. |
| Exceeds \$2,500 but does not exceed \$5,000 | Class I felony | Up to \$10,000 or imprisonment up to 3.5 years (18 months confinement, 2 years supervision), or both. |
| Exceeds \$5,000 but does not exceed \$10,000 | Class H felony | Up to \$10,000 or imprisonment up to 6 years (3 years confinement, 3 years supervision), or both. |
| Exceeds \$10,000 | Class G felony | Up to \$25,000 or imprisonment up to 10 years (5 years confinement, 5 years supervision), or both. |

DISCUSSION POINTS

UI Fraud

1. Claimants who conceal information from the Department of Workforce Development (DWD) when filing for benefits may be subject to repayment of benefits received, forfeiture of future benefits, penalty surcharges, and criminal prosecution. For UI purposes, to conceal means "to intentionally mislead or defraud the department by withholding or hiding information or making a false statement or misrepresentation." Some common examples of claimant fraud include: an individual who returns to work but continues to claim benefits; an individual who works part-time but does not report work performed and wages earned on the weekly claim certification; and claimants who falsify work search documents in an effort to receive benefits.

2. Pursuant to Wis. Stat. 108.14 (19), DWD must annually report to the Unemployment Insurance Advisory Council (UIAC) on the Department's activities related to detection and prosecution of UI fraud in the preceding year. From this report, the Department notes 13,034 cases of fraudulent overpayments to individuals in 2014. Fraudulent overpayments identified in 2014 totaled \$20.5 million of \$716.3 million in total benefits paid to claimants, or 2.9% of total payments.

3. Employers determined to have aided and abetted a claimant in committing an act of concealment or misrepresentation may be assessed an administrative penalty equal to the amount of the benefits the claimant improperly received as a result of the concealment, additional penalty assessments, and criminal penalties. An employer aids and abets a claimant when they have knowledge that a claimant is submitting or intending to submit a false claim and the employer either (a) renders aid to the claimant who submits a false claim, or (b) is ready and willing to render aid, if

needed, and the claimant who commits the concealment knows of the employing unit's willingness to aid in the concealment. In addition, the employer can be penalized \$500, \$1,000, and \$1,500 for each additional act of concealment.

4. UI fraud also includes employers who deliberately misclassify employees in an attempt to avoid paying UI taxes. Employers are required by law to correctly classify each worker as either an "employee" or "independent contractor." Worker classification determines whether or not the employer has legal obligations under the law for unemployment insurance, workers compensation, wage payments, work hours, record keeping and civil rights protections. If an employer is found to be utilizing misclassified workers, additional tax, interest and civil penalties, including the issuance of stop work orders, may result. Under state law, employers found to be engaged in employee misclassification can be fined not less than \$100 nor more than \$500, or imprisoned not more than 90 days or both. Also under current law, any construction employer who willfully provides false information to DWD for the purpose of misclassifying an employee of the employer as a nonemployee shall be fined \$25,000 for each violation. During 2014, DWD conducted 2,101 audits of employers, resulting in assessments totaling \$1.3 million. Auditors identified 4,709 misclassified workers during the 2,101 audits. The bill would not change these penalties for employer fraud.

Penalty surcharge

5. 2011 Wisconsin Act 198 created a 15% fraud surcharge effective October 21, 2012. From the effective date through October 20, 2013, revenues from these penalties were deposited into the program integrity fund, per state law. Effective October 21, 2013, federal law requires states to assess a fraud penalty of at least 15%, requiring the first 15% to be deposited into the state's UI trust fund. Collections of penalty monies on overpayments established after October 21, 2013, have been deposited in the UI trust fund. Table 2 shows \$2.6 million in total collections from the 15% UI fraud surcharge, including \$1.1 million credited to the program integrity fund and \$1.5 million credited to the UI trust fund. Penalty payments flowing into the program integrity fund will continue to be paid off over the next several years. Penalty payments flowing into the UI trust fund have grown as payment collections accrue from penalties established from October 21, 2013, to the present.

TABLE 2

History of UI Fraud Penalty Payment Collections

| <u>State Fiscal Year</u> | <u>Fraud Penalty Revenue from Penalties Established Between October 21, 2012 - October 20, 2013 (Deposited to UI Program Integrity Fund)</u> | <u>Fraud Penalty Revenue from Penalties Established Between October 21, 2013 - Present (Deposited to UI Trust Fund)</u> | <u>Total</u> |
|--------------------------|--|---|------------------|
| 2012-2013 | \$62,005 | | \$62,005 |
| 2013-2014 | 904,737 | \$394,331 | 1,299,068 |
| 2014-2015* | <u>142,818</u> | <u>1,118,247</u> | <u>1,261,065</u> |
| Total | \$1,109,560 | \$1,512,578 | \$2,622,138 |

*through 02/28/2015

6. Under the bill, the 15 percent penalty on certain fraudulent benefit payments erroneously paid to the claimant (overpayment) would increase to 40 percent. The administration's errata associated with this provision would clarify that proceeds from the 15 percent surcharge would be dedicated to the state's UI trust fund in accordance with federal law, while the remaining 25 percent would be dedicated to the state's program integrity fund. The administration also recommends a delayed effective date to allow time for computer programming needs. The delayed effective date would be October 4, 2015. Assuming an October 4, 2015, start-up date, it is estimated that the additional penalty revenue from the 25 percent surcharge would increase revenue into the state's program integrity fund by \$470,000 in 2015-16 and \$980,000 in 2016-17 [Alternative A1].

Criminal Penalties

7. Wisconsin law provides for the criminal prosecution of employees and employers participating in UI fraud. State law allows DWD to refer to local district attorneys and DOJ attorneys, cases that it believes may involve egregious fraudulent activity. The Department works with the appropriate District Attorney to get criminal charges filed against the offenders. DWD has indicated that it considers referring cases that involve overpayments of \$5,000 or more and include at least five allegations of concealment. DWD also uses other criteria, such as strength of available evidence, to select the specific cases referred for possible prosecution. The Department funds a 0.5 position at the Department of Justice to pursue such prosecutions. From 2011 through 2013, DWD referred 90 cases to district attorneys and the Department of Justice. As of October 2014, 67 of the 90 cases, or 74.4 percent, had been prosecuted and resulted in pleas of guilty or no contest. A total of 14 cases were pending, while the remaining nine cases were dismissed, not prosecuted, or resulted in deferred prosecution agreements.

8. In 2014, 19 cases were referred for state criminal prosecution. According to the Department, there is a disincentive to take these cases to court because penalties are too low. DWD believes that this is at least partly to blame for the low number of referrals, especially when

compared to the 13,034 cases of fraudulent overpayments identified by DWD in 2014. Department representatives have complained to the Unemployment Insurance Advisory Council (UIAC) about this reluctance to take on these cases. According to the Department, referrals for potential prosecution can take several years to resolve and do not always lead to convictions or even criminal charges. DWD has stated that the time that it takes to gather significant amounts of evidence on one case, refer the case to the local DA or state DOJ, wait for a charging decision and then wait for the case to work through the criminal court system toward a conclusion that could end in dismissal, deferment or a repayment order on par with what could have been pursued by the Department, it is reasonable that the Department considers other methods for collection and deterrence. It could be argued that an increase in penalties would help make concealment cases a higher priority for prosecutors [Alternative B1].

9. To the extent the criminal UI caseload for prosecutors would increase as a result of the provision, additional costs may be incurred by DWD's UI Division, local district attorneys, the Department of Justice, the State Public Defenders Office, State Courts and Corrections.

Concealment

10. Under the bill, penalties would increase for acts of concealment. However, there is significant disagreement between DWD and the Labor and Industry Review Commission (LIRC) over how to interpret the statutory definition of concealment. LIRC is an independent state agency responsible for deciding appeals of UI decisions issued by Department administrative law judges. According to the Department, after the Legislature enacted the definition of "conceal" in 2008, the Labor and Industry Review Commission (LIRC) interpreted the statutory definition of concealment more narrowly than was originally intended. The Department's position is that LIRC has interpreted the statute to not only require intent to mislead, but that DWD must also prove that the claimant provided false information with the intent to receive benefits to which they knew they were not entitled. In an April 9, 2015, memorandum from LIRC to the UIAC, LIRC strongly disagrees with the Department's characterization of LIRC's decisions as "narrowing" the concealment law and argues that the Commission consistently ruled that an act of concealment would be found only for willful acts of concealment and not due to ignorance or lack of knowledge and not where a claimant makes an honest mistake. Furthermore, LIRC states that the Commission's interpretation has been upheld in several recent Circuit Court decisions. This discord on the concealment issue has resulted in LIRC overturning a significant number of DWD determinations. Of the 196 concealment/fraud decisions issued by LIRC in 2014, 123 involved cases where DWD found fraudulent concealment that were subsequently reversed by LIRC.

11. A proposed UI law change drafted by the Department and currently before the UIAC would amend the statutory definition of "conceal" [Wis. Stat.108.04 (11)(g)] to eliminate the element of intent and create a rebuttable presumption that the claimant misled DWD when providing the false information to the Department in response to DWD's questions in the benefit claims process. It could be argued that modifying the statutory definition of concealment may be prudent prior to, or in conjunction with, any increase in penalties related to UI fraud, as proposed in the budget bill. Absent a modification, an increase in UI fraud penalties may only serve to increase the amount of litigation. The Committee could choose to delete the increased penalties from the

budget bill and refer the matter to the UIAC for possible inclusion in the Council's agreed upon bill. This option would also allow for additional public input and fiscal estimates to be submitted by affected public agencies. [Alternative A2 and B3].

12. The Committee could also choose to add language to the budget bill to modify the definition of concealment. However, if the definition of concealment is substantially similar to the Department's March 19, 2015, draft proposal, the law may encounter a number of legal problems. In the opinion of LIRC, the proposal contains a presumption of fraud which creates due process concerns and may not survive judicial scrutiny, may be at odds with the U.S. Department of Labor's interpretation of fraud and concealment, and negates the state's common law on the issue of what constitutes concealment for the purposes of UI fraud. Finally, the Commission warns that such a proposal could result in substantial criminal fraud penalties for honest mistakes.

Other Considerations

13. Increased civil and criminal penalties for UI fraud were not previously considered by the Unemployment Insurance Advisory Council. The state's UI law establishes a UIAC to advise DWD in carrying out the purpose of Wisconsin's unemployment insurance law. The Council is composed of five employer and five employee representatives who are appointed by the Secretary of DWD to serve six-year terms. The UIAC can submit its recommendations for changes in UI law to the Legislature and report its views on any other pending legislation which relates to UI. The Council generally presents an "agreed upon" bill for consideration by the Legislature in the fall of each odd-numbered year. Historically, the Council's recommended changes in UI law presented to the Legislature have been adopted with few, if any, amendments. In 2013, the Governor and subsequently Joint Finance and the Legislature made significant changes to the state's UI law through the budget process. The Governor's initial recommendation, followed by the Legislature's amendments to modify UI law through the 2013 budget (Act 20) was a significant departure from the process as described above for how the Council's recommended changes to UI law had historically been presented to the Legislature.

14. Other states impose a wide range of civil and criminal penalties for UI fraud. As of 2013, 15 states were identified as having criminal penalties which included felony charges specifically for UI fraud. In most other states, including Wisconsin, prosecutors use existing state and federal theft, forgery and fraud laws to bring about felony charges for UI fraud cases deemed most serious. In upper Midwestern states, Michigan, Illinois, Minnesota and Iowa have no specific state felony laws targeting UI fraud but certain cases are prosecuted as felonies under existing theft, welfare fraud and forgery laws. In Indiana, criminal penalties for UI fraud refer to the state's welfare fraud statutes which are as follows: misdemeanor fine of up to \$1,000 and imprisonment up to one year if \$250 or less, felony fine of up to \$10,000 and imprisonment up to three years if over \$250 but less than \$2,500, and felony fine of up to \$10,000 and imprisonment for two through eight years if greater than \$2,500.

ALTERNATIVES

A. Civil penalties

1. Approve the Governor's recommendation, as corrected, to increase the surcharge to 40% beginning on October 4, 2015, or the Sunday after publication, whichever is later. Specify that the current 15% surcharge would be deposited to the state's UI trust fund and the additional 25% surcharge would be deposited to the state's program integrity fund.

2. Delete provision (maintain the current law 15% surcharge).

B. Criminal penalties

1. Approve the Governor's recommendation for increased criminal penalties for UI fraud as detailed in Table 1.

2. Delete the changes to criminal penalties. Penalty modifications could be considered by the UIAC for possible inclusion in the Council's regular 2015-16 legislative session bill, which may also include a provision modifying the definition of "concealment."

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