



Testimony on House Bill 5407 (an act establishing a tax credit for employers that provide paid family and medical leave benefits and a family and medical leave accounts program)

Submitted by Scott Shepard, Policy Director

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Good afternoon. My name is Scott Shepard. I am the Policy & Research Director for the Yankee Institute for Public Policy, Connecticut's free-market think tank. I submit this note in support of **House Bill 5407**.

Saving against the possibility of a debilitating illness – for oneself or a family member, or in anticipation of a birth or adoption, or for related contingencies, is an extremely wise move. Getting assistance in this process from employers who can afford to help is both a good in itself and a valuable spur to put the money aside. Where the state can efficiently and economically afford to, as with a tax credit, it should provide incentives for employers to help and practical assistance for them in their efforts to do so.

We support **House Bill 5407** because it incorporates this vision of economically assisting people to care for themselves with an eye toward a healthy and successful future.

This bill stands in stark contrast to **Senate Bill 1** and **House Bill 5003**. Those bills would mandate a 0.5 percent payroll tax for all employees to fund a \$1,000/week paid FMLA benefit for all workers for up to 12 weeks per year every year. Leaving aside philosophical considerations about the proper role of government, there is one key distinction between **House Bill 5407** and those two bills: **House Bill 5407**, if drawn correctly, should work well. **Senate Bill 1** and **House Bill 5003**, on the other hand, bear almost no chance of ending as anything other than extremely costly failures.

The mean annual wage in Connecticut is somewhat less than \$60,000/year.¹ Because that average includes all income, not just the amount below the payroll-tax threshold, using it for these purposes technically (even if only in the short term) overestimates the

¹ See https://www.bls.gov/oes/current/oes_ct.htm.

amount of revenue that will be generated by this tax.² Using it, nevertheless, for simplicity's sake yields this result: the average Connecticut worker will pay \$300/year as a result of the initial 0.5 percent payroll tax. Assuming very conservative administrative costs for the program of 10 percent of collections and benefit payments, it will take 44 workers' payroll taxes to support one worker's full use of the FMLA benefit each year.

It follows, then, that if just 2.27 percent of workers take full advantage of paid FMLA – and no one else takes any FMLA time at all – the program will nevertheless go broke almost immediately at a 0.5 percent payroll tax and sink further into the red every year from there.

This means that the state will have to start hiking this payroll tax almost as soon as it starts paying benefits. How high will it get? That depends on how many workers take partial or full advantage of the FMLA benefit each year.

It's not clear what the initial use rate will be. We can expect the rate to be fairly high, however, because under the proposed legislation, the benefit would pay out *100 percent of a worker's weekly wage*, up to a total of \$1,000 per week for 12 weeks per year. This higher payment will induce more people to use the benefit than otherwise would, which in turn will drive up the costs of the program, which in turn will drive up the payroll tax.

Consider this close comparison. Many employers offer sick days. These sick days usually offer full compensation for the day(s) missed, but with a limit on use of much less than 12 weeks a year. Assume that the average employee has five sick days a year. Now assume that the average employee uses, again on average, just one of those sick days every year. That represents a 20 percent use of sick days. If FMLA use rises to 20 percent, then the payroll tax will have to rise by nearly 9 times, to nearly 4.5 percent. At 4.5 percent the average Connecticut worker would pay \$2,700 per year in state FMLA payroll tax – more in FMLA payroll tax than in state income tax.

² That figure decreases somewhat because the current proposal would charge the payroll tax on income only up to the Social Security maximum, which is now (in 2019) \$132,900. See https://www.ssa.gov/policy/docs/quickfacts/prog_highlights/index.html. Because that cap will be raised automatically upon fund shortfalls, however, we don't expect it to remain in place for long. See proposed S.B. 1 § 2(c)(1)-(3) (2019). (The legislature has designed this legislation so that the base upon which the payroll tax will operate will rise automatically to meet the needs of the program, without the legislature having to vote for – and thus take responsibility for – those tax increases. Instead, increases in the top amounts subject to the payroll tax will occur automatically upon a determination of the administrator of the program that such increases are necessary to the solvency of the program, unless the legislature votes down the increase by a three-fifths vote. Because we expect this to happen almost immediately, we also expect that this initial exclusion is effectively meaningless once benefit distributions start.)

There are a variety of reasons to believe that use won't reach 20 percent, especially right away. But even very constrained use will require increases in the payroll tax or bankruptcy of the fund. And as the payroll tax rises, inhibitions against using the benefit – and a desire to get something back for those increasingly burdensome deductions – will rise. This suggests markedly increased use of the benefit over time, and a spiral of ever-increasing payroll deductions.

From this, we conclude that Connecticut's paid FMLA benefit, as currently structured, will likely very quickly become unstable, resulting in ever-rising payroll taxes even as benefits are slashed and the program itself veers into bankruptcy. We have not seen any effort by the state of Connecticut realistically to demonstrate that this level of payroll tax can possibly support this level of benefit into a sustainable future. If the state were to undertake such a calculation, we would need it to show its work carefully; the state hardly has an impressive track record of properly calculating the cost benefit programs and funding them accordingly. But in this instance it appears not even to have tried.

HB 5407 is simply not susceptible to this debilitating and unexamined series of pitfalls. It does its work with a tax credit, which is to say by allowing businesses to keep a little more of their revenue to help them to establish and support these paid FMLA programs and accounts. In turn, thoughtful employees receive incentives to save for themselves. **HB 5407** does not create any under-contribution problems, any spiraling cost cycles, or any constant ratcheting up of payroll taxes on hardworking Connecticut citizens – with all of the business- and family-flight effects we know will follow from such consistent and significant tax hikes.

HB 5407 does a noble thing in a thoughtful and affordable way. We support it.