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ADVISORY: UNEMPLOYMENT INSURANCE PROGRAM LETTER NO. 2-09

TO: STATE WORKFORCE AGENCIES

FROM: BRENT R. ORRELL *Brent R. Orrell*
Deputy Assistant Secretary

SUBJECT: Recovery of Unemployment Compensation Debts Due to Fraud from Federal Income Tax Refunds

1. Purpose. To inform states of recent amendments to Federal law authorizing the recovery of certain unemployment compensation (UC) debts due to fraud from Federal income tax refunds.
2. References. Public Law 110-328, the "SSI Extension for Elderly and Disabled Refugees Act;" the Social Security Act (SSA); the Internal Revenue Code (IRC), including the Federal Unemployment Tax Act (FUTA); and Unemployment Insurance Program Letter (UIPL) 22-96 (61 Fed. Reg. 27101 (May 30, 1996)).
3. Background. On September 30, 2008, the President signed Public Law 110-328, the "SSI Extension for Elderly and Disabled Refugees Act." Among other things, this Act amended Federal law to permit the states to recover certain UC debts due to fraud from Federal income tax refunds under the "Treasury Offset Program" (TOP) operated by the United States Department of the Treasury (Treasury).

Under TOP, Treasury collects certain delinquent Federal and state debts by intercepting Federal income tax refunds. The amendments authorize Treasury to expand the TOP program to intercept certain UC debts related to fraud. Although the amendments apply to refunds payable on or after the date of enactment, it is anticipated that Treasury will issue regulations prior to implementing UC TOP. The current thinking is that UC TOP will be implemented by using the Interstate Connection Network and that Treasury would deposit any amounts intercepted directly into the state's account in the Unemployment Trust Fund (UTF).

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Although participation in UC TOP is optional for states, the Department of Labor (DOL) strongly encourages participation as the program is expected to be an effective means of recovering UC debts.

States interested in participating in UC TOP have asked if any amendments to state law are necessary as a condition of participating. This UIPL provides a general overview of the Federal amendments and the anticipated design of the UC TOP program. Questions regarding state amendments are addressed in Item 6. Additional guidance will be issued as needed.

A copy of P.L. 110-328 is attached; therefore, references to particular provisions of the enactment are omitted.

4. Debts Collectible under UC TOP. As amended by Public Law 110-328, Federal law now authorizes the use of TOP for collecting a “covered unemployment compensation debt” (“covered UC debt”). This term means:

- A past-due debt for erroneous payment of UC due to fraud which has become final under the state’s UC law and which remains uncollected for not more than 10 years;
- Contributions due to the unemployment fund of a state for which the state has determined the person to be liable due to fraud and which remain uncollected for not more than 10 years; and
- Any penalties and interest (P&I) assessed by the state on the above debts.

An offset may be made under UC TOP only if the individual is filing a Federal income tax return from the state seeking the offset. Specifically, UC TOP may be used only if the address shown on the Federal return for the taxable year for which the refund is being made is an address within the state seeking the offset.

5. The UC TOP Process. Preliminary discussions with Treasury indicate that UC TOP will likely be designed as follows:

- A state will establish UC debts under existing state law and initiate normal collection activities.
- The state UC agency may use UC TOP for collecting covered UC debts if the conditions described below are met. Because state participation is voluntary, participating states have latitude in determining whether all or some of these debts would be referred to UC TOP.

- Submission of covered UC debts to Treasury for collection is subject to the following:
 - Treasury regulations may specify the time and manner in which states are to submit collection requests, including any minimum dollar amount for individual debts.
 - Treasury regulations may require that the state has “made reasonable efforts to obtain payment” of the covered UC debt.
 - A requirement that the state must notify the debtor by certified mail return receipt that it plans to recover the debt through the offset of any Federal tax refund. The notice must give the debtor at least 60 days to present evidence that all or part of the liability is either not legally enforceable or due to fraud. The state must consider any evidence presented and determine that the amount of the debt is legally enforceable and due to fraud. The state must also satisfy any other conditions that Treasury imposes.
- Treasury will match the collection requests from the UC agency against any Federal income tax refunds due.
- Upon establishing a match, Treasury will:
 - Determine if the address shown on the Federal return for the year of the refund is within the state seeking the offset. If it is, Treasury will deduct the debt from the income tax refund due the debtor after any higher priority debts are paid. Higher priority debts are Federal taxes, past-due child support, and past-due legally enforceable debt owed to a Federal agency. If there is more than one UC debt collection request against a Federal income tax refund, the refund will be applied against the UC debts in the order in which the debts accrued. (Similarly, if a state is using TOP to collect a state income tax debt, the refund will be applied in the order in which the UC and state income tax debts accrued.)
 - Deduct any Treasury or DOL fees from the amount of debt collected. These fees are intended to cover any costs Treasury and DOL incur in the operation of the UC TOP program.
 - Transmit the debt offset from income tax refunds (less fees) to the state’s account in the UTF and notify the state of the person’s name, taxpayer identification number, address and the amount collected. Note that the amount deposited in the UTF may include P&I that is owed state funds; in such cases, states may transfer such P&I “to the appropriate State fund into which the State would have deposited such amounts had the person owing the debt paid such amounts directly to the

State.” (Section 3304(a)(4)(G)(ii), FUTA, as amended.)

- Notify the debtor that his/her refund has been reduced by an amount necessary to satisfy a debt. In the case of a joint return, the notice will include information related to the rights of the spouse of the taxpayer subject to the offset.
- If an amount has been erroneously intercepted and paid to a state’s unemployment fund, the state will be sent a notice of the erroneous payment and will be required to pay Treasury an amount equal to the amount of the erroneous payment.

6. UC TOP Issues for State Law.

- a. Authority to Use UC TOP. Whether a state’s law authorizes use of UC TOP for recovering covered UC debts (including both debts to the state’s unemployment fund and P&I) is a matter to be determined under the state’s law.
- b. Notice of Determination. As described above, before using UC TOP to collect a covered UC debt, a state is required to determine that the debt is legally enforceable and due to fraud, after affording the debtor at least 60 days to present evidence.

At a minimum, the state must establish procedures to notify the debtor that the debt is subject to offset, receive and evaluate the evidence provided, and determine whether the debt is legally enforceable and due to fraud. This required opportunity to present evidence is not a review of the initial determination establishing the overpayment or other liability. Instead, it provides the UC debtor an opportunity to demonstrate that the amount is not subject to recovery through UC TOP, thereby minimizing erroneous intercepts. If, as a result of the review, it is determined that the debt is not legally enforceable or due to fraud, UC TOP may not be used. The UC TOP legislation does not require the state to amend its initial determination.

Whether states will need to amend their UC laws to establish procedures or whether the state agency can establish procedures through rules or other administrative process is a matter to be determined by each state. In any case, the procedures must be consistent with any rules Treasury issues.

- c. Payment of Administrative Fees.

As discussed above, administrative fees will be deducted from the amounts collected through the offset. States should examine their laws to determine if they may assess administrative fees and add them to the covered UC debt. The result would be that 100% of the covered UC debt will be returned to the state, and the debtor would pay any additional processing costs through a further reduction to any tax refund.

Otherwise, amounts to pay administrative fees may be withheld from the debts themselves. Whether a state needs to seek amendment to its law to authorize this withholding depends on the fund to which the debt is due.

From Amounts Due P&I Fund. Federal requirements restricting the use of unemployment fund moneys do not apply to the use of P&I that are required by state law to be paid into a separate P&I account. (See UIPL 22-96, item 5.c.) As a result, if state law permits, states may pay administrative fees from any P&I collected through UC TOP.

From Amounts Due Unemployment Fund. Public Law 110-328 amended FUTA's "withdrawal standard" to provide that "amounts may be deducted [from intercepted tax refunds] to pay any fees" authorized under the UC TOP law. (Section 3304(a)(4)(G)(i), FUTA.) Since state laws are written to conform to Federal law, they limit the use of unemployment fund moneys to the payment of UC and other purposes authorized by Federal law. As a result, it is anticipated that states will need to amend their laws to specifically permit unemployment fund moneys to be used for payment of fees related to UC TOP. One option for amending state laws is to add an authorization to the definition of "unemployment fund" which permits withdrawals for "payment of fees authorized under the Treasury Offset Program described in Section 6402(f) of the Internal Revenue Code."

Concerning unemployment fund moneys, it should be noted that, under UC TOP, Treasury acts on the state's behalf in recovering amounts due the state's unemployment fund. Under the "immediate deposit" requirement, such amounts are "in" the unemployment fund at the instant of the intercept. (See UIPL 22-96, which discusses the application of the immediate deposit requirement of Section 303(a)(4), SSA, and Section 3304(a)(3), FUTA, as well as the "withdrawal" standard.) As a result, states may not use these amounts for any purpose other than the payment of UC or other purposes authorized by Federal law.

d. Effect of Withholding of Administrative Fees from Debts. If the administrative fee is withheld from money due the unemployment fund or P&I, situations will occur where the entire debt is not satisfied through UC TOP. For example:

- A state submits a \$1,000 fraud overpayment for collection through UC TOP.
- Treasury intercepts \$1,000 from the debtor's Federal income tax refund and deducts, for purposes of an example, \$35 in Treasury and DOL fees.
- \$965 is deposited in the state's unemployment fund.

Since nothing in Federal law explicitly addresses this situation, it is DOL's position that it is a matter of state law whether the state is required to credit the debtor with the full \$1,000 intercepted to pay the fraud overpayment.

Similarly, nothing in Federal law addresses how this situation affects the charging of overpayments to employers in states where an overpayment remains charged to the employer's account until such time as the state's unemployment fund is made whole. Although the UC TOP provisions do not require the employer to be relieved of such charges, as a matter of equity, DOL suggests that the states permit such relief since the employer is generally not responsible for the administrative costs incurred in collecting the debt.

7. Termination Date. The authority to recover covered UC debt from Federal income tax refunds expires on September 30, 2018, the date which is 10 years after the date of enactment of Public Law 110-328.
8. Action Required. State administrators should distribute this advisory to appropriate staff.
9. Inquiries. Please direct inquiries to the appropriate Regional Office.
10. Attachment. Section 3 of Public Law 110-328.

TEXT OF SECTION 3 OF P.L. 110-328

An Act

To amend section 402 of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 to provide, in fiscal years 2009 through 2011, extensions of supplemental security income for refugees, asylees, and certain other humanitarian immigrants, and to amend the Internal Revenue Code of 1986 to collect unemployment compensation debts resulting from fraud.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the `SSI Extension for Elderly and Disabled Refugees Act.* * *

SEC. 3. COLLECTION OF UNEMPLOYMENT COMPENSATION DEBTS RESULTING FROM FRAUD.

(a) In General- Section 6402 of the Internal Revenue Code (relating to authority to make credits or refunds) is amended by redesignating subsections (f) through (k) as subsections (g) through (l), respectively, and by inserting after subsection (e) the following new subsection:

`(f) Collection of Unemployment Compensation Debts Resulting From Fraud-

`(1) IN GENERAL- Upon receiving notice from any State that a named person owes a covered unemployment compensation debt to such State, the Secretary shall, under such conditions as may be prescribed by the Secretary--

`(A) reduce the amount of any overpayment payable to such person by the amount of such covered unemployment compensation debt;

`(B) pay the amount by which such overpayment is reduced under subparagraph (A) to

such State and notify such State of such person's name, taxpayer identification number, address, and the amount collected; and

`(C) notify the person making such overpayment that the overpayment has been reduced by an amount necessary to satisfy a covered unemployment compensation debt.

If an offset is made pursuant to a joint return, the notice under subparagraph (C) shall include information related to the rights of a spouse of a person subject to such an offset.

`(2) PRIORITIES FOR OFFSET- Any overpayment by a person shall be reduced pursuant to this subsection--

`(A) after such overpayment is reduced pursuant to--

`(i) subsection (a) with respect to any liability for any internal revenue tax on the part of the person who made the overpayment;

`(ii) subsection (c) with respect to past-due support; and

`(iii) subsection (d) with respect to any past-due, legally enforceable debt owed to a Federal agency; and

`(B) before such overpayment is credited to the future liability for any Federal internal revenue tax of such person pursuant to subsection (b).

If the Secretary receives notice from a State or States of more than one debt subject to paragraph (1) or subsection (e) that is owed by a person to such State or States, any overpayment by such person shall be applied against such debts in the order in which such debts accrued.

`(3) OFFSET PERMITTED ONLY AGAINST RESIDENTS OF STATE SEEKING OFFSET- Paragraph (1) shall apply to an overpayment by any person for a taxable year only if the address shown on the Federal return for such taxable year of the overpayment is an address within the State seeking the offset.

`(4) NOTICE; CONSIDERATION OF EVIDENCE- No State may take action under this subsection until such State--

`(A) notifies by certified mail with return receipt the person owing the covered unemployment compensation debt that the State proposes to take action pursuant to this section;

`(B) provides such person at least 60 days to present evidence that all or part of such liability is not legally enforceable or due to fraud;

`(C) considers any evidence presented by such person and determines that an amount of such debt is legally enforceable and due to fraud; and

`(D) satisfies such other conditions as the Secretary may prescribe to ensure that the determination made under subparagraph (C) is valid and that the State has made reasonable efforts to obtain payment of such covered unemployment compensation debt.

`(5) COVERED UNEMPLOYMENT COMPENSATION DEBT- For purposes of this subsection, the term 'covered unemployment compensation debt' means--

`(A) a past-due debt for erroneous payment of unemployment compensation due to fraud which has become final under the law of a State certified by the Secretary of Labor pursuant to section 3304 and which remains uncollected for not more than 10 years;

`(B) contributions due to the unemployment fund of a State for which the State has determined the person to be liable due to fraud and which remain uncollected for not more than 10 years; and

`(C) any penalties and interest assessed on such debt.

`(6) REGULATIONS-

`(A) IN GENERAL- The Secretary may issue regulations prescribing the time and manner in which States must submit notices of covered unemployment compensation debt and the necessary information that must be contained in or accompany such notices. The regulations may specify the minimum amount of debt to which the reduction procedure established by paragraph (1) may be applied.

`(B) FEE PAYABLE TO SECRETARY- The regulations may require States to pay a fee to the Secretary, which may be deducted from amounts collected, to reimburse the Secretary for the cost of applying such procedure. Any fee paid to the Secretary pursuant to the preceding sentence shall be used to reimburse appropriations which bore all or part of the cost of applying such procedure.

`(C) SUBMISSION OF NOTICES THROUGH SECRETARY OF LABOR- The regulations may include a requirement that States submit notices of covered unemployment compensation debt to the Secretary via the Secretary of Labor in accordance with procedures established by the Secretary of Labor. Such procedures may require States to pay a fee to the Secretary of Labor to reimburse the Secretary of Labor

for the costs of applying this subsection. Any such fee shall be established in consultation with the Secretary of the Treasury. Any fee paid to the Secretary of Labor may be deducted from amounts collected and shall be used to reimburse the appropriation account which bore all or part of the cost of applying this subsection.

(7) ERRONEOUS PAYMENT TO STATE- Any State receiving notice from the Secretary that an erroneous payment has been made to such State under paragraph (1) shall pay promptly to the Secretary, in accordance with such regulations as the Secretary may prescribe, an amount equal to the amount of such erroneous payment (without regard to whether any other amounts payable to such State under such paragraph have been paid to such State).

(8) TERMINATION- This section shall not apply to refunds payable after the date which is 10 years after the date of the enactment of this subsection.'

(b) Disclosure of Certain Information to States Requesting Refund Offsets for Legally Enforceable State Unemployment Compensation Debt Resulting From Fraud-

(1) GENERAL RULE- Paragraph (3) of section 6103(a) of such Code is amended by inserting '(10),' after '(6).'

(2) DISCLOSURE TO DEPARTMENT OF LABOR AND ITS AGENT- Paragraph (10) of section 6103(l) of such Code is amended--

(A) by striking '(c), (d), or (e)' each place it appears in the heading and text and inserting '(c), (d), (e), or (f)',

(B) in subparagraph (A) by inserting ', to officers and employees of the Department of Labor for purposes of facilitating the exchange of data in connection with a request made under subsection (f)(5) of section 6402,' after 'section 6402', and

(C) in subparagraph (B)--

(i) by inserting '(i)' after '(B)'; and (ii) by adding at the end the following:

(ii) Notwithstanding clause (i), return information disclosed to officers and employees of the Department of Labor may be accessed by agents who maintain and provide technological support to the Department of Labor's Interstate Connection Network (ICON) solely for the purpose of providing such maintenance and support.'

(3) SAFEGUARDS- Paragraph (4) of section 6103(p) of such Code is amended--

(A) in the matter preceding subparagraph (A), by striking '(1)(16),' and inserting '(1)(10), (16),';

(B) in subparagraph (F)(i), by striking '(1)(16),' and inserting '(1)(10), (16),'; and

(C) in the matter following subparagraph (F)(iii)--

(i) in each of the first two places it appears, by striking '(1)(16),' and inserting '(1)(10), (16),';

(ii) by inserting '(10),' after 'paragraph (6)(A),'; and

(iii) in each of the last two places it appears, by striking '(1)(16)' and inserting '(1)(10) or (16)'.

(c) Expenditures From State Fund- Section 3304(a)(4) of such Code is amended--

(1) in subparagraph (E), by striking 'and' after the semicolon;

(2) in subparagraph (F), by inserting 'and' after the semicolon; and

(3) by adding at the end the following new subparagraph:

'(G) with respect to amounts of covered unemployment compensation debt (as defined in section 6402(f)(4)) collected under section 6402(f)--

'(i) amounts may be deducted to pay any fees authorized under such section; and

'(ii) the penalties and interest described in section 6402(f)(4)(B) may be transferred to the appropriate State fund into which the State would have deposited such amounts had the person owing the debt paid such amounts directly to the State;'.

(d) Conforming Amendments-

(1) Subsection (a) of section 6402 of such Code is amended by striking '(c), (d), and (e),' and inserting '(c), (d), (e), and (f)'.

(2) Paragraph (2) of section 6402(d) of such Code is amended by striking 'and before such overpayment is reduced pursuant to subsection (e)' and inserting 'and before such

overpayment is reduced pursuant to subsections (e) and (f)'.

(3) Paragraph (3) of section 6402(e) of such Code is amended in the last sentence by inserting `or subsection (f)' after `paragraph (1)'.

(4) Subsection (g) of section 6402 of such Code, as redesignated by subsection (a), is amended by striking `(c), (d), or (e)' and inserting `(c), (d), (e), or (f)'.

(5) Subsection (i) of section 6402 of such Code, as redesignated by subsection (a), is amended by striking `subsection (c) or (e)' and inserting `subsection (c), (e), or (f)'.

(e) Effective Date- The amendments made by this section shall apply to refunds payable under section 6402 of the Internal Revenue Code of 1986 on or after the date of enactment of this Act.