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Beginner's Guide to Unemployment Insurance for Small Business

By Sue Marquette Poremba, Business News Daily Contributing Writer April 20, 2018 07:02 am EST

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No one plans to lose their job. However, that's exactly what happens when a small business owner decides to close their doors to retirement, relocation or poor sales. Employees quickly become former employees and are suddenly in search of new careers. Unemployment insurance allows those former employees some sense of financial security.

However, there is a lot of misunderstanding around unemployment insurance, such as who pays for the insurance benefits, who is eligible for them and whether you can opt out of providing this benefit. Below is a guide that should answer some of the basic questions about unemployment insurance.

A brief history

Unemployment insurance came into effect nationwide as part of the Social Security Act of 1935 as a way to assist the unemployed during the Great Depression and its recovery. It is a [federally mandated and regulated program](#), but eligibility and payment amounts are determined at a state level.

In most states, unemployment insurance is funded through taxes employers pay on behalf of their employees (although in some states, [the employees pay this tax directly](#)). These taxes are directed to a state-controlled reserve fund.

"The employer reserve fund, which is made up of 3 to 7 percent of an employee's gross wages depending on the individual state, is backed by a reserve fund controlled by the state," said Jim Bell Sr., founder and CEO of Abel HR in Cranbury, New Jersey. "If that fails, the federal government lends money to ensure unemployed workers are paid. All businesses must pay into unemployment insurance, except for certain nonprofits."

The concept of the original unemployment insurance benefit continues to run in a similar manner to its 1935 inception; however, over the years, more rules, regulations and reports have been added. Also, the unemployment division now covers payments for disability, Family and Medical Leave Act claims, workforce development, re-employment, and enforcement.

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Who must pay unemployment insurance?

Companies of every size need to worry about unemployment insurance, especially small businesses.

"One of the biggest misconceptions held by many business owners and managers is that unemployment insurance is a fixed, uncontrollable tax," said Bell. "This concept could not be further from the truth. Unemployment insurance costs can be controlled from the moment a business starts."

The state determines a three-year startup contribution to unemployment and disability insurances for new businesses. After three years, the rate is averaged to calculate the next year's payment and then is annually re-evaluated.

From hire to termination

Generally, whenever a company hires an employee, part of the new hire process includes enrollment in either the state, federal or both unemployment compensation programs. Depending on the state's requirements, new hires are periodically reported and placed on the tax rolls.

"Subsequently, each time an employee has payroll taxes deducted, from each paycheck, some of that money is used for the unemployment compensation insurance pool," explained Charles A. Krugel, human resources attorney and counselor. "Depending on the state where the employer or employee is located, benefits-eligible people will receive a biweekly or monthly payment based on a formula based mainly on the employee's rate of pay, cost of living and other statutory factors."

Most states have at-will employment laws, meaning both the employee and the employer can either leave or be terminated at any time for any reason that is not illegal. At-will employees are eligible for unemployment. The exception is if the departure is due to a disciplinary problem such as insubordination, theft and other serious charges.

When a termination does occur, be sure to keep detailed documentation that protects the company if a claim is filed, denied and challenged.

"Documentation is key," said Krugel. "When documenting, [a] business should write up incidents as soon as they occur. That is, document who was involved, who witnessed what, where events occurred, when events occurred, what happened, why do you think it happened, and so on."

In-depth advice

The steps for handling the unemployment insurance can usually be found on each state department's website, according to Chris Orletski, co-president of Blankit Insurance Group. "More often, this is becoming an online process whereby the employer uploads the required information to the state, but, again, an employment attorney would be able to advise appropriately."

Orletski also advised any employer with unemployment insurance and tax questions to turn to an employment attorney in the state which you intend to employ individuals. The secretary of state's website usually provides a direct link to the department charged with handling the unemployment insurance for that state.

"The overall takeaway is that unemployment insurance is not handled by insurance agencies, but by a state governmental agency," said Orletski.



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