# Memorandum

To: Panel Members

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From: Maureen Reilly
General Counsel

File: Panel Memo

Subject: Out-of-State Competition

In this Memo, staff proposes an expanded approach to determining Out-of-State Competition (OSC), which is an important aspect of eligibility for all employers, including participants in a Multiple Employer Contract. The issue was previewed in my remarks last month. (Panel Meeting Minutes, May 2016.)

## ISSUE

**Should ETP accept web-based delivery of goods or services in determining OSC, as a formal expression of Panel policy?**

Web-based delivery was not a consideration in the early years of determining OSC some two decades ago, when use of the Internet was not a common business practice. Over time, staff began accepting web-based delivery case-by-case, especially for Industry Sectors where it was an integral part of the business model (e.g., Professional Services; Finance and Insurance; Internet Publishing.) However, case-by-case analysis is fact-specific, and the outcomes can be varied or even inconsistent.

Web-based delivery is becoming more of an issue as businesses are increasingly marketed and operated over the Internet, including social media such as Facebook and Pinterest. Even Small Business in California competes in a global market today. However, the ETP legislation and regulations are silent on this subject, and there is no clear policy direction.

[Note: Although there is no clear policy on web-based delivery, the Panel has traditionally funded Retail Trade as Special Employment Training (SET), even though Internet sales have been common in that Industry Sector for many years. Under SET, employers in Retail Trade have been held to the highest post-retention wage standard. See discussion of SET Wage on page 2.]

## BACKGROUND

The requirement for OSC is statutory. It dates back to an amendment enacted in January 1994, a decade after ETP was created. OSC was added to other program mandates under the "purpose" provisions of Unemployment Insurance Code (UI) Section 10200 as shown in the excerpt below:

> (a) California's economy is being challenged by competition from other states . . . [The Panel] shall fund only projects that meet the following criteria:
>
> > (1) Foster creation of high-wage, high-skilled jobs, that are threatened by out-of-state and global competition,....or foster retention of high-wage, high-skilled jobs in manufacturing and other industries,……………………………..…………………..

The Panel interpreted OSC in regulation Section 4416, originally adopted in 1996 and amended in 2006. The regulation identifies Industry Sectors that are “deemed to meet” OSC based on the North American Industry Classification System (NAICS). This includes all of Manufacturing, and 14 Ancillary Codes. Eligibility for these employers is not subject to case-by-case analysis for any location.

[Note: There are “carve outs” to accept OSC for Mortgage Banking and two other industries: Call Centers and Destination Resorts. These industries are an exception to SET funding even if they are not found to have OSC in the first stage of analysis, with separate determination criteria for each.]

SET was created in 1994 at the same time as the requirement for OSC, at new UI Code Section 10214.5. For employers without OSC, this is the only source of core program funding, capped at 15% of availability per FY. The statute is targeted to “frontline workers” earning at least the Statewide Average Hourly Wage (SET Wage). In 1997, the Panel interpreted SET in regulation Section 4409. Section 4409 limits training to frontline workers only, and mandates the SET Wage. It was amended in 2010 to allow a “wage modification” for Priority Industries and Critical Proposals, case-by-case.

**The SET Wage is higher than other ETP wage requirements: $28.37 ($21.28 if modified) in 2016.**

## SUMMARY

The statute and regulations are silent on the issue of web-based delivery in determining OSC. This concept does not appear in ETP guidelines, orientation/marketing materials, funding applications or queries. However, the analysis of OSC is becoming almost impossible to sustain in today’s Internet-driven economy without a policy decision on whether to accept web-delivery of goods or services.

Many employers can readily demonstrate OSC through web-based delivery. For example, most of Retail Trade would be removed from SET. If so, it can be expected that more employers in that Sector would apply for funding. If this is not the Panel’s intent, then web-based delivery could be excluded for Retail Trade; and/or that Sector could be designated as Lowest Priority under the Strategic Plan for FY 2016/17. The Strategic Plan is subject to periodic review and adjustment throughout the FY.

Web-based delivery would not affect funding for Industry Sectors that are geographic-specific, such as Healthcare and Construction. Those two Sectors have traditionally been funded as SET. However, they are also Priority Industries eligible for the modified SET Wage per Section 4409.

[Note: Regardless of web-based delivery, Mortgage Banking would remain “carved out” for OSC. In light of remarks made at last month’s meeting, if that is not the Panel’s intent, this industry could also be designated as Lowest Priority; again, in connection with adopting the FY 2016/17 Strategic Plan.]

## RECOMMENDATION

Option 1: Continue case-by-case analysis under the existing statutory and regulatory framework, but accept web-based delivery as a form of competition in determining OSC for all Industry Sectors.

Option 2: The same as Option 1 but do not accept web-based delivery for Retail Trade Sector 44-45, which would remain eligible for SET funding. This Sector could also be considered for Lowest Priority, pending further research and data analysis. This Sector includes auto and other dealership sales.

Staff recommends that any action taken today should be prospective only for funding in FY 2016/17. This would apply to proposals on today’s Agenda, but only those identified as ET17. Proposals still in development may need a re-determination of eligibility, but active contracts would not be affected.