

NOTE

RECOVERY OF UNEMPLOYMENT INSURANCE OVER-PAYMENTS: THE ROLE OF EQUITY AND GOOD CONSCIENCE

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INTRODUCTION

Section 597.4 of the New York State Unemployment Insurance Law¹ gives the state a right to recover erroneously paid unemployment benefits after a determination is made either to decrease or deny them.² The state may compel claimants who followed the prescribed procedures to repay benefits that were overpaid because of state error.³ Consequently, the statute enables the state to correct its own bureaucratic errors at the claimant's expense, even if the claimant cannot afford to repay. Prior to the statute's amendment in 1983, it permitted recovery only when the overpayments were caused by the claimant's bad faith, false statement, or wilful concealment regarding any fact pertinent to the benefits claim.⁴

1. N.Y. LAB. LAW § 597.4 (McKinney Supp. 1984).

2. Throughout this Note, the terms "recovery" and "recoupment" will be used interchangeably to denote the state's action to retrieve overpayments or erroneous payments of benefits. While recoupment technically refers only to withholding of a claimant's future benefits, the term is also frequently used to refer to orders for repayment. *See, e.g.,* *Kominski v. Levine*, 50 A.D.2d 346, 377 N.Y.S.2d 700 (1975), *aff'd*, 42 N.Y.2d 843, 366 N.E.2d 81, 397 N.Y.S.2d 381 (1977). *See generally* Annotation, *Repayment of Unemployment Compensation Benefits Erroneously Paid*, 90 A.L.R.3d 987, 991 (1979) (discussion uses recoupment and repayment interchangeably). *But see* FLA. STAT. § 443.151(6)(b) (1983) (distinction made between repayment and recoupment). For a discussion of the judicial treatment of this distinction, see *infra* note 59. In this Note, recoupment will be used to refer to both repayment orders and withholding of future benefits.

3. *See* *Claim of Palsyn*, 100 A.D.2d 716, 717 n.2, 474 N.Y.S.2d 609, 610-11 n.2 (1984).

4. *E.g., Kominski*, 50 A.D.2d at 350, 377 N.Y.S.2d at 705.

In contrast to New York, other states have statutes that explicitly prohibit recovery when such recovery would offend notions of equity and good conscience.⁵ Some states that do not provide an explicit statutory exception do provide common law protection for good faith recipients.⁶ For example, the Supreme Court of Delaware implies a fairness requirement and allows the state to recoup nonfraudulent overpayments only when equitable considerations "preponderate" in the State's favor.⁷

This Note will argue that a state should not have the automatic right to recover overpayments which result from its own errors. Recoupment should be based on the equities of each case. The New York statute discourages unemployed workers from using their benefits because they fear they will be forced to repay them later. To remedy this inhibition, the current statute should be amended or, at the very least, be interpreted by the courts to protect claimants from liability for state errors. This Note will present methods for advocates of the unemployed to challenge statutes similar to New York's in administrative hearings and in the courts.

I

THE HISTORY AND STRUCTURE OF UNEMPLOYMENT INSURANCE

A. *The Federal Scheme*

The present unemployment compensation system originated in the Social Security Act of 1935.⁸ Enacted as a response to the economic collapse of the Great Depression, the Social Security Act attempts to remedy the predominant causes of poverty: unemployment, dependency in old age, loss of the family wage earner, and illness.⁹ A purpose of the Act is to provide unemployed workers with short term relief; unemployed workers should not be forced to resort to charity, welfare, or their life savings while searching for a new job.¹⁰ The structure Congress established to fulfill this goal delegates the onus of administering unemployment insurance to the states. A state is eligible for federal grants if its laws conform with the requirements of the Social Security

5. See, e.g., CAL. UNEMP. INS. CODE § 1375 (Deering 1985) which provides: Any person who is overpaid any amount as benefits under this part is liable for the amount overpaid unless:

(a) The overpayment was not due to fraud, misrepresentation or wilful nondisclosure on the part of the recipient, and
(b) The overpayment was received without fault on the part of the recipient, and its recovery would be against equity and good conscience.

6. See, e.g., *Snead v. Unemployment Ins. Appeals Bd.*, 486 A.2d 676 (Del. 1984); *Galvin v. Iowa Beef Processors, Inc.*, 261 N.W.2d 701, 703-04 (Iowa 1978); *Martinez v. Texas Employment Comm'n*, 570 S.W.2d 28 (Tex. Civ. App. 1978).

7. *Snead*, 486 A.2d at 680; see *infra* text accompanying notes 74-77.

8. Act of Aug. 14, 1935, ch. 531, 49 Stat. 626, (codified as amended at 42 U.S.C.A. §§ 501-504 (West 1983 & West Supp. 1987)).

9. S. REP. NO. 628, 74th Cong., 1st Sess. 2 (1935).

10. H.R. REP. NO. 615, 74th Cong., 1st Sess. 7 (1935).

Act¹¹ and the Federal Unemployment Tax Act.¹²

The determination of a claimant's eligibility for unemployment compensation is not based on need; rather, benefits are awarded to individuals who demonstrate that they were involuntarily unemployed through no fault of their own.¹³ The money to pay these benefits comes from those employers who are statutorily required to "contribute" to the state's unemployment insurance fund. The sum contributed by each employer is determined in most states (including New York) by the employer's "experience rating," the amount paid from the fund to the employer's former employees during the previous year.¹⁴

B. The New York Statutory Scheme

The New York Unemployment Insurance Law was enacted on April 23, 1935, several months prior to the enactment of the Social Security Act.¹⁵ In its Declaration of Public Policy, the statute parallels federal concerns regarding the evils of unemployment:

"Economic insecurity due to unemployment is a serious menace to the health, welfare, and morale of the people of this state. Involuntary unemployment is therefore a subject of general interest and concern which requires appropriate action by the legislature to prevent its spread and to lighten its burden, which now so often falls with crushing force upon the unemployed worker and [her] family [T]he legislature therefore declares that in its considered judgment the public good and the well-being of the wage earners of this state require the enactment of this measure for the compulsory setting aside of financial reserves for the benefit of persons unemployed through no fault of their own."¹⁶

The statute assigns authority over the collection, administration, and disbursement of these "financial reserves" to the industrial commissioner, who wields wide-ranging powers to effectuate the policies behind the statute.¹⁷

An individual claimant begins the process of applying for benefits by filing a claim with the local state employment office serving the area in which she was last employed or in which she resides.¹⁸ The claimant must declare herself "totally unemployed" and must regularly report to the employment

11. 42 U.S.C.A. § 503(a) (West Supp. 1985).

12. 26 U.S.C.A. § 3304 (West 1983).

13. NATIONAL EMPLOYMENT LAW PROJECT, INC., LEGAL SERVICES GUIDE TO FEDERAL UNEMPLOYMENT COMPENSATION LAWS AND ISSUES 1-2 (1977) [hereinafter LEGAL SERVICES GUIDE].

14. *Id.* at 14.

15. See UNEMPL. INS. REP. (CCH) N.Y. ¶ 4,000.

16. N.Y. LAB. LAW § 501 (McKinney 1977).

17. *Id.* at §§ 530-39.

18. *Id.* at § 596.1.

office in the event that work is available.¹⁹ The commissioner at the local office makes the initial determination of the claim's validity and determines the amount of benefits payable to the claimant.²⁰ Within one year of the initial determination, the local office may review it to consider new or corrected information. Review is not available, however, if the case has been adjudicated at a hearing or an appeal.²¹

Initial determinations may be appealed by either the claimant or her employer(s) to an administrative law judge (ALJ), who holds an evidentiary hearing concerning the claim.²² Rules of evidence or procedure need not be strictly observed; however, all parties involved in the hearing must be afforded a full opportunity to present pertinent testimony and evidence.²³ Decisions by an ALJ may be appealed to the Appeal Board,²⁴ which usually bases its review upon the factual record compiled in the ALJ hearing. This decision may then be appealed to the appellate division of the state supreme court, third department, which also tends to base its review on the existing evidentiary record and to limit its inquiry to questions of law.²⁵ Finally, the decision of the appellate court may be reviewed by the court of appeals, which is likewise generally constrained in its scope of review.²⁶

Before 1983, New York courts tended to interpret the statutory good faith provision sympathetically to claimants. For example, in *Matter of Valvo*,²⁷ the court of appeals considered section 597.4 where a claimant failed to report to the unemployment office that she occasionally wrote a few checks for her employer while she was laid off. The court held that although Ms. Valvo was not "totally unemployed" within the meaning of the statute — and thus ineligible for benefits²⁸ — she could not have realized that her activities constituted employment. The state was barred from recovering her benefits because she did not act in bad faith, but merely erred in her interpretation of the law.²⁹ The court reasoned that "when [a] claimant has in good faith received benefits to which [she] was not entitled because of a mistake of law on the part of the claimant or the agency, none of the benefits may be recovered."³⁰ Such an interpretation, according to the court, was required by the wording of the statute and supported by the legislative history.³¹ The court

19. *Id.* at § 596.2.

20. *Id.* at § 597.1.

21. *Id.* at § 597.3. When fraud or wilful misrepresentation is present, the time limit of § 597.3 is not applicable. *See In Re Marder*, 16 A.D.2d 303, 227 N.Y.S.2d 730 (1962).

22. N.Y.COMP. CODES R. & REGS. tit.12, § 461 (1985).

23. *Id.* at § 461.4(a).

24. N.Y. LAB. LAW § 621. The board has discretion under § 621 to hear arguments, hold a further hearing, or remand the case to an ALJ.

25. *Id.* at § 624.

26. *Id.*

27. 57 N.Y.2d 116, 440 N.E.2d 780, 454 N.Y.S.2d 695 (1982).

28. *See* N.Y. LAB. LAW § 522.

29. 57 N.Y.2d at 127-28, 440 N.E.2d at 785-86, 454 N.Y.S.2d at 700-01.

30. *Id.* at 128, 440 N.E.2d at 786, 454 N.Y.S.2d at 701.

31. *Id.* The court in *Valvo* also considered the cases of two additional claimants who

considered it unfair to compel a person without any other resources to repay benefits to which she honestly believed she was entitled.³²

The version of section 597.4 passed by the New York Legislature in 1983 removed such good faith restrictions on state recovery. Now, whenever a review of an initial determination or an appeal results in a decrease or denial of benefits, the commissioner has a right to recover the money paid pursuant to the initial determination.³³ This amendment of section 597.4 was part of a larger revision of the unemployment insurance and workers' compensation laws³⁴ that, in the words of Governor Mario Cuomo, would "effectuate cost-saving measures and eliminate inequitable provisions of the law[s]."³⁵ In his memorandum approving the bill, the Governor stated that strengthening the industrial commissioner's recovery powers would "insure that only legitimately qualifying claimants receive . . . benefits."³⁶

Governor Cuomo's comments contain two common assumptions that pervade general discussion of the recoupment issue. They are, first, that failure to recover overpayments will destroy the unemployment insurance system's fiscal solvency and, second, that allowing undeserving claimants to keep erroneously paid benefits contravenes the purpose of unemployment compensation.³⁷ While these general concerns with cost and equity may be valid — and will be discussed later³⁸ — policy considerations may outweigh them.

II

WHY PROTECT GOOD FAITH CLAIMANTS?

The state's desire to recover the amount of funds paid to claimants as a result of state error is legitimate. However, the New York statute's blanket

worked during periods of alleged unemployment. One claimant "performed essentially the same limited services while allegedly unemployed as she did while allegedly employed;" the other was warned that her activities constituted employment. *Id.* at 126-27, 440 N.E.2d at 785, 454 N.Y.S.2d at 700. The court concluded that the state could reasonably infer that these claimants knew that their activities constituted employment. Hence, the state's determination that they were liable for the overpayments under § 597.4 was valid because they falsely stated their employment status. *Id.*

32. See also *Abatematteo v. Levine*, 51 A.D.2d 846, 380 N.Y.S.2d 350 (1976) (recovery of overpayment deprived plaintiff of equal protection of law). In coming to its decision, the *Abatematteo* court relied upon *Kominski v. Levine*, 50 A.D.2d 346, 377 N.Y.S.2d 700 (1975), *aff'd*, 42 N.Y.2d 843, 366 N.E.2d 81, 397 N.Y.S.2d 381 (1977). In *Kominski*, the court was faced with a statute — later repealed — that allowed recoupment of benefits received by a claimant pending an appeal that ultimately reversed the claimant's eligibility. The court found that, in light of § 597.4's requirement of bad faith, false statements, or concealment, equal protection required a hearing similar to that granted claimants ordered to repay under § 597.4. *Id.* at 350, 377 N.Y.S.2d at 705.

33. See *Claim of Palsyn*, 100 A.D.2d 716, 717 n.2, 474 N.Y.S.2d 609, 610-11 n.2 (1984).

34. Act of June 30, 1983, ch. 415, § 9, 1983 N.Y. Laws 775, 784. The bill, among other things, increased benefits and made the experience rating system permanent. See Memorandum of State Executive Department, 1983 N.Y. Laws 2529, 2530.

35. Memorandum of the Governor, 1983 N.Y. Laws 2768, 2768-69.

36. *Id.*

37. 90 A.L.R.3d at 991.

38. See *infra* Section III.

grant of authority to the commissioner to recover overpayments of benefits, regardless of fault or need, fails to address situations where it would be absolutely unfair to demand recovery. The following hypotheticals, based on actual cases, demonstrate some of these situations:

1) Claimant *X* quit her job in reaction to a suspension notice which she believes is unfair. *X*, however, neglected to go through the grievance procedure at her job, and thereby failed to take sufficient steps towards saving her position. Such actions would normally be classified as "voluntarily leaving one's job without good cause" and would be sufficient grounds for denying benefits. However *X*, unsure whether she qualifies for benefits, goes to the local employment office to inquire about her eligibility. At the office, *X* is not interviewed by a claims officer. Instead, an office employee directs *X* to register the following week at a benefits window where she will receive a check. In fact, over the next few months, *X* receives weekly checks totalling more than \$1,200, which she uses for food, rent, and clothing for herself and for her family. Meanwhile, pursuant to section 597.3, the state determines that *X* was in fact not eligible for the benefits that she received; pursuant to section 597.4, it institutes an action for recovery of the money. *X*, who has already used the money and who is still out of work, must now pay back the benefits.

2) Claimant *Y* is fired by her employer under unfriendly circumstances. *Y* goes to her local employment office and is interviewed by a claims officer. The claims officer determines that *Y* is entitled to benefits, which *Y* then begins to receive. The claims officer, however, fails to contact the employer who, upon learning that *Y* is receiving benefits, informs the state that she fired *Y* for misconduct, thereby disqualifying *Y* from receiving benefits. The state issues a new determination, and soon *Y* is confronted with an adverse judgment and a demand for repayment, even though she complied in good faith with all the regulations of the unemployment insurance statute.

These hypotheticals demonstrate that the strict provisions of the New York recovery statute fail to consider the plight of those who have in good faith complied with the unemployment insurance scheme yet are later charged with the burden of repaying benefits. Critics of the good faith exception argue that claimants should not be allowed to retain any benefits to which they were never entitled. They argue that eligibility for unemployment insurance is not based on financial need.³⁹ Therefore, the recipient's need for benefits should not be considered when the state acts to recover overpaid benefits.⁴⁰

39. See LEGAL SERVICES GUIDE, *supra* note 13.

40. See NATIONAL COMM'N ON UNEMPLOYMENT COMPENSATION, RESPONSE TO PROPOSALS ON BASIC STRUCTURE OF FEDERAL-STATE UNEMPLOYMENT INSURANCE PROGRAM AND RELATED SUPPORTING PROVISIONS 243 (1979) [hereinafter COMMISSION RESPONSES] (comments of David A. Pearson, Wisconsin Department of Industry, Labor, and Human Relations). In his comments, Mr. Pearson, responding to a commission proposal concerning recoupment waiver, claimed that recoupment "should be tailored to the individual's ability to repay." However, he asserted that there are no "social rights" entitling a claimant to retain overpaid benefits, because unemployment compensation is based on "insurance principles." *Id.*

Nevertheless, while a claimant's need is not part of the initial eligibility determination, a different analysis should be utilized in determining whether an overpayment has occurred and whether the claimant is obligated to repay. Equity and good conscience require courts and administrative agencies to be true to the socio-economic goals of the unemployment insurance program and to examine the claimant's financial position before demanding repayment. A poor claimant who acted in good faith is simply incapable of repaying the overpayment. If forced to repay, she is punished for relying on the unemployment system. This result violates the intent of the unemployment insurance program.

A need-based analysis for unemployment compensation finds justification in several court decisions. An Illinois appellate court in *Meadows v. Grabiec*⁴¹ examined the disproportionate impact on indigents of an anti-fraud provision in the state unemployment insurance law. The statute required claimants found guilty of defrauding the unemployment insurance system to repay all benefits received pursuant to the fraudulent activity before they could be considered eligible again for benefits. The court held that the state's refusal to allow a claimant to offset future benefits against the overpayment violated the equal protection clause of the fourteenth amendment. Poor people, if required to repay the overpayment before requalifying for benefits, would be prevented from requalifying in a disproportionate number to those people with adequate resources.⁴² The court held that the statute be interpreted to allow the offsetting of future benefits as an alternative remedy to requiring immediate payment.⁴³ By introducing a repayment system based on financial need, the court established a system that more accurately reflects the anti-poverty aims underlying unemployment insurance.⁴⁴ An equitable result can also be attained in New York by protecting those good faith recipients who would suffer serious harm if compelled to repay overpayments.

A second argument against allowing retention of overpaid benefits is based on fiscal concerns. The argument is that the unemployment system is under such financial strain that it cannot afford to allow overpayments to remain uncollected. According to a 1980 study by the National Commission of Unemployment Compensation, overpayments constituted 18.47% of all benefit payments in six major American cities, of which approximately 22% were due to agency error.⁴⁵ Furthermore, as one commentator has observed, a large number of states have borrowed federal funds to offset deficiencies in their

41. 20 Ill. App. 3d 407, 314 N.E.2d 283 (1974).

42. *Id.* at 413, 314 N.E.2d at 288.

43. *Id.* at 414-15, 314 N.E.2d at 289.

44. *Id.* See also *California Human Resources Dep't. v. Java*, 402 U.S. 121 (1970) (Douglas, J., concurring). Justice Douglas, disputing that unemployment insurance benefits are not based on need, stated that "history makes clear that the thrust of the scheme for unemployment benefits was to take care of the need of displaced workers." *Id.* at 135.

45. NATIONAL COMM'N ON UNEMPLOYMENT COMPENSATION, FINAL REPORT 108 (1980).

collection-payment ratios.⁴⁶ Recovery of benefits alleviates some of the strain on unemployment insurance systems. However, the more fundamental threat to solvency is not overpayments, but the failure of states to increase unemployment insurance tax rates to match increases in benefit levels, inflation, and unemployment.⁴⁷ Raising tax rates to realistic levels is a much more potent and farsighted way to promote solvency than is indiscriminate, counter-productive recoupment.

A third argument for recoupment maintains that allowing claimants who acted in good faith to keep overpaid benefits harms employers.⁴⁸ Employers' unemployment insurance tax burdens are determined by the amount of unemployment insurance previously paid to their former employees. The main thrust of this argument is that employers will be charged for erroneous payments made to their former employees and, consequently, will face undeservingly higher tax rates.⁴⁹ The New York statute, however, makes clear that modifications and corrections of the employer's experience rating charges depend on *decisions* concerning the claimant's ineligibility, not on the money that is paid or recouped.⁵⁰ Overpayments do not affect the solvency of the employer and thus should not bar protecting good faith recipients.

III

RECOVERY POLICIES IN OTHER STATES

Unlike New York, a number of states have statutory provisions which protect claimants who have erroneously received benefits through no fault of their own. Nine states⁵¹ have explicit provisions in their unemployment insurance statutes which forbid assignment of liability to a claimant for overpayments received without fraud, misrepresentation, or nondisclosure where recovery of the overpayments would offend equity and good conscience. Nine other states⁵² provide that recovery may be waived at the commission's discretion when it would be offensive to both the purposes of unemployment insur-

46. Padilla, *The Unemployment Insurance System: Its Financial Structure*, 104 MONTHLY LAB. REV. 32 (Dec. 1981).

47. *See id.*; Becker, *The Location of Financial Responsibility in Unemployment Insurance*, 59 U. DET. J. URB. L. 509, 511-12 (1982). *See also* Meadows v. Grabiec, 20 Ill. App. 3d 407, 414, 314 N.E.2d 283, 288-89 (rejecting state's argument that allowing future recoupment instead of repayment would deplete state funds).

48. *See* COMMISSION RESPONSES, *supra* note 40 at 145 (comments of Bruce King, Governor of New Mexico).

49. *Cf. id.* Governor King claimed that states cannot waive overpayments because of the "reimbursable employers." If a waiver was allowed, the equitable response to these employers would be to reimburse them in order to keep their taxes at appropriate levels.

50. N.Y. LAB. LAW § 581.6 (McKinney 1977). *See also* Carleson v. California Unemp. Ins. Appeal Bd., 64 Cal. App. 3d 145, 134 Cal. Rptr. 278 (1976) (erroneously paid benefits do not affect employers who are charged by either the experience rating method or by the reimbursement method).

51. Az., Ark., Cal., Fla., Haw., Mass., Neb., Nev., Wyo. *See* U.S. Dep't of Labor, Pub. No. 450.01, COMPARISON OF STATE UNEMPLOYMENT INSURANCE LAWS (1984) [hereinafter COMPARISON].

52. Ala., Colo., Ill., La., Mich., N.C., N.D., S.D., Wash. *See id.*

ance and equitable considerations. Courts in these states have generally read into these broad equity provisions a prohibition of recovery from benefits erroneously received through no fault of the claimant.

In *Gilles v. Department of Human Resources Development*,⁵³ the California Supreme Court determined whether equity and good conscience⁵⁴ were violated by the state agency's practice of justifying recoupment solely on the ground that the recipient had timely notice of possible future liability. Six claimants were discharged by their employers for alleged misconduct. The claimants applied for and, after favorable initial determinations, were awarded benefits. The former employers appealed those decisions. The state sent notices to the claimants concerning the appeals that advised them of their potential liability for overpayments. The claimants chose to continue receiving benefits while the appeals were pending. The appeal held claimants ineligible for benefits. The state then tried to recover the benefits received while the appeals were pending.

The California Supreme Court unanimously held that the state could not recover the benefits merely because it gave the claimants notice of their potential liability. In addition to notice, equity and good conscience required consideration of such matters as: the cause of the overpayment, whether benefits paid were normal benefits — thereby weighing against recovery — or extra, duplicative ones — thereby weighing in favor of recovery, whether the claimants changed their position in reliance upon receipt of benefits, and whether recovery of overpayments would tend to defeat the objectives of the unemployment insurance code by imposing extraordinary hardship on the claimant.⁵⁵ The court held that neglecting these equitable concerns would defeat the two purposes underlying the statute and the federal law⁵⁶ regarding unemployment compensation. It saw these purposes as providing benefits for persons unemployed through no fault of their own, and reducing involuntary

53. 11 Cal.3d 313, 521 P.2d 110, 113 Cal. Rptr. 374 (1974).

54. CAL. UNEMP. INS. CODE § 1375 (Deering 1985).

55. 11 Cal.3d at 323, 521 P.2d at 117, 113 Cal. Rptr. at 380-81.

56. The court found support for its interpretation of § 1375 in federal court decisions interpreting § 204 of the Social Security Act, 42 U.S.C.A. § 404 (1983), which also prohibits recovery when it would violate the purpose of the statute or offend equity and good conscience. The court claimed that:

The decisions of the federal courts interpreting that section make no attempt to lay down specific standards for recovery, but decide the issue on a case by case basis, taking into account the origin of the overpayment, the extent to which the recipient changes his position in reliance on the receipt of benefits, and the impact of recoupment upon the recipient's current financial position.

Id. at 323, 521 P.2d at 117, 113 Cal. Rptr. at 381 (footnotes omitted).

The court later discussed federal law in regard to the plaintiffs' contention that withholding of future benefits would violate the "when due" provision of the Social Security Act, 42 U.S.C.A. § 503(a)(1) (1983). While the court rejected the plaintiffs' assertion, it did reiterate that "federally administered social security and unemployment compensation programs permit recoupment, by means of setoff or civil action, *only when such recoupment will not defeat the statutory purpose nor contravene equity and good conscience.*" *Id.* at 328, 521 P.2d at 120, 113 Cal. Rptr. at 384 (emphasis by the court).

unemployment and suffering caused thereby to a minimum.⁵⁷ The court stated that "[s]imply putting money into the worker's hands will neither alleviate the hardship of unemployment nor maintain purchasing power if that worker feels obligated to hold that sum intact until final conclusion of the appeal."⁵⁸ The court did allow the possibility that the state could recoup overpayments by withholding future benefits; but it warned that such an action should be undertaken cautiously with an eye towards the purpose of the statute and any equitable concerns.⁵⁹

In a concurring opinion, Justice William P. Clark, Jr., compelled by what he perceived as "the increased frequency of recoupment proceedings," proposed changing the procedural requirements of recoupment actions.⁶⁰ To Clark, the state's proof of notice should constitute "a *prima facie* showing that extenuating circumstances precluding repayment do not exist;" the claimant should have the burden of demonstrating that requiring repayment is unconscionable.⁶¹ Clark believed that this would be both fair and efficient since the claimant was in a better position than the state to know of the circumstances that should prohibit repayment. Such a system of proof would save state resources by cutting its arduous investigatory task of disproving that recoupment would not violate equity and good conscience.⁶²

The *Gilles* court's interpretation of "equity and good conscience" has been accepted by several states with equity and good conscience provisions. In *Giles v. Director of Labor*,⁶³ an Arkansas court found that the claimant's poor financial position barred state recovery. The claimant received food stamps, both he and his wife were unemployed, he could not pay his rent, and he could not afford to repair his broken car.⁶⁴

Even states without explicit statutory good faith exceptions to recovery

57. 11 Cal.3d at 316, 521 P.2d at 112, 113 Cal. Rptr. at 376 (citing CAL. UNEMP. INS. CODE § 100).

58. *Id.* at 325, 521 P.2d at 118, 113 Cal. Rptr. at 382. It should be noted that *Gilles* has also been adopted by the Ninth Circuit. See discussion of *Hanley v. Donovan*, *infra* note 87.

59. *Id.* at 328, 521 P.2d at 120, 113 Cal. Rptr. at 384; accord *Schmidt v. Industrial Comm'n*, 42 Colo. App. 253, 600 P.2d 76 (1979). In Florida, there is an interesting dispute among the district courts of appeal as to whether the equity and good conscience provision of the state recovery statute, which is contained in the subsection dealing with withholding of future benefits, also applies to repayment orders. See FLA. STAT. § 443.151 (6) (1983). The Third District, in decisions such as *Sagaert v. State*, 418 So. 2d 1228 (Fla. Dist. Ct. App. 1982) and, most recently, in *Renelus v. Florida Unemployment Appeals Comm'n*, 484 So. 2d 629 (Fla. Dist. Ct. App. 1986) (per curiam), has found that equity and good conscience must be extended to repayment orders. Such a result, according to the court, is necessary in order to avoid the "illogical" result of providing waivers only for one method of recovery while denying it for another. See *Sagaert*, 418 So. 2d at 1230. The Fourth District, however, has taken a more literal view of the statute and has denied application of equitable waiver to repayment orders. See *Sheppard v. State*, 442 So. 2d 1114, 1116 (Fla. Dist. Ct. App. 1983).

60. *Id.* at 329-30, 521 P.2d at 121, 113 Cal. Rptr. at 385.

61. *Id.*

62. *Id.*

63. 621 S.W.2d 10 (Ark. Ct. App. 1981).

64. *Id.* at 11.

have protected good faith recipients. In *Galvin v. Iowa Beef Processors, Inc.*,⁶⁵ strikers were advised by Iowa's Employment Security Commission to file for unemployment benefits even though they were also receiving union strike benefits. The commission advised the strikers to file so that the strikers would be able to retain their benefits if they were found eligible for them. The commission initially determined that the claimants were entitled to benefits. The employer's appeal to the commission — allowed despite its lateness — reversed the initial determination.

The Iowa Supreme Court agreed with the commission that the claimants were ineligible for the received benefits. Nonetheless it prohibited the state from recovering. The court held that the claimants should not be required to repay benefits which would have been final and unrecoverable⁶⁶ had the court not entertained the employer's appeal after the statutorily provided time limit. The court interpreted the recoupment statute, which provided for recovery of overpayments made as a result of "any error,"⁶⁷ as inapplicable to good faith recipients who committed no errors of their own. A contrary reading of legislative intent would "force workers to either await prolonged litigation . . . or to pay back at some remote later date benefits already received and used for family support."⁶⁸ This contrary interpretation negates the purpose of the state's unemployment insurance act: to minimize the "crushing burden" of unemployment.

In *Martinez v. Texas Employment Commission*,⁶⁹ a Texas court employed a similar analysis. The plaintiff lacked wages sufficient to qualify for benefits. The commission mistakenly paid him benefits based on the record of another employee. When the commission discovered the error, it demanded repayment under a statute that allowed recovery whenever overpayment resulted from "nondisclosure or misrepresentation."⁷⁰ The Court of Civil Appeals reversed the district court's affirmation of the commission's repayment order. It held that the discretionary provision in the statute applied to the *form* of repayment, not to the *equities* of repayment.⁷¹ In other words, the commission only had discretion with respect to how to achieve repayment. The commission could demand a current repayment of overpaid benefits or deduct from future benefits but the commission had no discretion to forgive repayment. However, the court did hold for the claimant. It noted the "remedial" nature of the Texas Unemployment Compensation Act: to provide relief to "the economic plight of people who are unemployed through no fault of their own."⁷² The

65. 261 N.W.2d 701 (Iowa Sup. Ct. 1978).

66. *Id.* at 704.

67. *Id.*

68. *Id.* It should be noted that the Iowa legislature placed an equity provision in its statute in response to *Galvin*, but subsequently enacted a recovery provision much like New York's. See IOWA CODE ANN. § 96.3 (7) (West 1984).

69. 570 S.W.2d 28 (Tex. Ct. Civ. App. 1978).

70. TEX. LAB. CODE ANN. § 5221b-14(d) (Vernon 1971).

71. 570 S.W.2d at 31.

72. *Id.* at 32.

court barred recovery of the benefits overpaid because of state error.⁷³

Delaware's *Snead v. Unemployment Insurance Board*⁷⁴ provides the most sweeping defense of good faith recipients in a state without an explicit equitable bar on recovery. In *Snead*, the claimant was awarded benefits in a referee hearing, at which the employer failed to appear despite having received proper notice. The employer then appealed the referee's decision. The Appeals Board reversed the referee and ordered the claimant to pay back \$1,076 in benefits which she had received prior to the appellate hearing. The Delaware Supreme Court overturned the lower court's affirmance of the Appeals Board. The court held that requiring repayment would cause "one who is not guilty of any fraud [to] receive unemployment benefits at his or her peril, since the [Delaware] Department of Labor may retroactively recover all sums paid when an award is later disallowed."⁷⁵ This would violate the purpose of unemployment compensation: "tid[ing] an unemployed worker over until he or she acquires a new job."⁷⁶ The court found an implied prohibition on recovery of nonfraudulent payments except when "equitable considerations preponderate in the State's favor."⁷⁷ The court concluded that: "In the final analysis principles of equity must prevail, so that there is not added to the devastation of unemployment the icy fear that an unreasoning government lurks to enhance the terrible pressure wrought by the loss of a job."⁷⁸

IV

RECOMMENDATIONS FOR NEW YORK

A. *Call for Legislative Change*

The preceding section demonstrates that equity and good conscience considerations protect claimants who, despite good faith compliance with the statute and/or agency, erroneously received benefits and are unable to repay them. The purpose of unemployment compensation is to provide the unemployed with sufficient resources to feed, clothe, and house themselves and their families while they look for work. The courts that protect claimants from repaying erroneous benefits received in good faith are primarily motivated by a desire to be true to this purpose.⁷⁹ These courts have also been sensitive to the "chilling effect" an unfettered state power to recover overpayments would cause. The unemployed would naturally be hesitant to exercise their right to receive benefits if the state had that power. This "chilling" harms not only the unemployed workers and their families, but also decreases buying power in the economy, particularly in periods of high unemployment.⁸⁰

73. *Id.*

74. 486 A.2d 676 (Del. Supr. 1984).

75. *Id.* at 678.

76. *Id.* at 680.

77. *Id.*

78. *Id.* at 681.

79. See *supra* notes 55-78 and accompanying text.

80. See *Gilles v. Department of Human Resources Dev.*, 11 Cal. 3d 313, 325, 521 P.2d

The New York Legislature, in light of these considerations, must amend section 597.4 to include an equity and good conscience provision. The amendment would return the unemployment insurance system to its original spirit and establish a system where, as articulated by the *Snead* court, claimants are free from future threats of substantial financial hardship.⁸¹

Courts may imply protection for good faith benefit recipients, as *Galvin*, *Martinez*, and *Snead* demonstrate. However, the courts, acting on their own, cannot be relied on to guarantee this protection. Courts might read very narrow exceptions for good faith protection into unemployment insurance statutes. These exceptions may not cover the wide range of real life situations. Also, courts may refuse to read *any* good faith exception into statutes that do not include one. In *Martinez*, for example, the court rejected an equity exception — grounding its decision, instead, on its interpretation of “misrepresentation” — and indicated that it would not protect claimants against recoupment under a statute like New York’s.⁸² Other courts, such as the Ohio Supreme Court, take a much more strict view of statutes lacking equity provisions: the plain language of such statutes totally precludes any examination of equitable concerns.⁸³ These decisions indicate that New York must amend its statute to include explicit protections for good faith recipients of benefits rather than rely on the courts to do so.

B. Court Challenges

Representatives of the unemployed can invoke estoppel and due process to persuade ALJ’s and courts to bar the recoupment of overpaid unemployment benefits resulting from state error. These challenges will stimulate practitioners to search for creative methods to attack the statute and, thereby, protect the interests of good faith recipients.

In *Wells v. Everett*,⁸⁴ an Arkansas court estopped the state from recovering benefits after a claimant verified her eligibility for the benefits with the state. The claimant took her initial benefit check to the local employment office and expressed her doubts about her eligibility to an office employee. The employee confirmed her eligibility. Six months later the state discovered that she should not have been paid and demanded that she repay the benefits, despite the fact that her only other source of income was Social Security. The agency’s board of review upheld this determination and asserted that repay-

110, 118, 113 Cal. Rptr. 374, 382. The court explained that neither the hardship of being unemployed would be relieved nor would purchasing power be maintained by a situation where the “worker feels obligated to hold [her benefits] until the final conclusion of the appeal.” *Id.*

81. See *Snead v. Unemployment Ins. Appeal Bd.*, 486 A.2d 676, 680-681 (Del. 1984). The court stated that this fear “stands the unemployment compensation laws on its head.” It mandated that workers “are not to be put in the untenable position of innocently receiving unemployment benefits at their peril.” *Id.* at 680.

82. See *Martinez v. Texas Employment Comm’n*, 570 S.W.2d 28, 31, 32 (Tex. Ct. Civ. App. 1978).

83. *Parks v. Garnes*, 49 Ohio St. 2d 251, 254, 361 N.E.2d 1057, 1059 (1977).

84. 5 Ark. App. 303, 635 S.W.2d 294 (1982).

ment did not offend equity and good conscience.⁸⁵ The Arkansas appellate court held the state could not recover the payments for the following reasons: the state knew the facts of the claimant's case, the state intended the claimant to act on its determination of eligibility, the claimant did not know she was ineligible, and the claimant relied on the state's determination to her detriment.⁸⁶

However, estoppel is problematic because courts may decide to follow long-standing precedent and refuse to allow the defense against government bodies. The Ninth Circuit warned that estoppel should be exerted against the government only when the moving party proves both the government's failure to inform and its affirmative misconduct.⁸⁷ Claimants fighting state recovery of unemployment benefits may have difficulty proving these incidents.

Claimants may also assert their due process rights as a bar to state recovery of erroneously paid benefits. In *Howard v. Board of Review*,⁸⁸ a New Jersey appellate court halted the state's attempt to recover benefits even though the unemployment insurance statute contained no equity and good conscience provision. The court held that due process mandates that the claimant have a "meaningful opportunity to present 'all available defenses' and arguments" concerning the equities of the refund order.⁸⁹

Although *Howard* aids advocates of the unemployed, courts sometimes reject due process claims in states without equity and good conscience provisions. In *Tucker v. Caldwell*,⁹⁰ the Fifth Circuit held that because Georgia's recoupment statute lacked an equity and good conscience provision, the claimant's due process rights were satisfied by the hearing to determine whether there was an overpayment.⁹¹

Even in states that mandate considerations of equity in guaranteeing due process, the criteria used to decide the claim may nullify the right. In *Vasquez v. Horn*,⁹² a New Jersey court upheld guidelines that permitted the state to waive recovery only when the overpayment was the result of agency error, or the client did not commit fraud *and* was dead or permanently disabled.⁹³ The court held the limitations valid because they were rational and consistent with the purposes of unemployment compensation.⁹⁴

85. *Id.* at 304-05, 635 S.W.2d at 294-95.

86. *Id.* at 306, 635 S.W.2d at 295.

87. *Hanley v. Donovan*, 734 F.2d 473 (9th Cir. 1984).

88. 173 N.J. Super. 196, 413 A.2d 976 (1980).

89. *Id.* at 203, 413 A.2d at 980. For a more detailed discussion of due process considerations, see National Employment Law Project, *Recoupment of Overpayments of Unemployment Compensation*, 14 CLEARINGHOUSE REV. 432 (1980); Note, *Unemployment Compensation — Waiver and Recoupment of Overpayments*, 7 MEM. ST. U.L. REV. 683 (1977).

90. 608 F.2d 140 (5th Cir. 1979).

91. *Id.* at 144-45.

92. 181 N.J. Super. 529, 438 A.2d 570 (1981).

93. *Id.* at 533, 438 A.2d at 572.

94. *Id.* at 535-38, 438 A.2d at 574-76.

V
CONCLUSION

The current version of the New York recoupment statute perpetrates great injustice on recipients of unemployment compensation benefits who have been overpaid or who have been erroneously paid as a result of bureaucratic error. In contrast to New York, a number of state courts and legislatures, driven by a desire to maintain procedures reflecting the spirit of federal and state unemployment insurance statutes and to encourage unemployed workers to use the system, apply principles of equity and good conscience to the recovery process. These efforts have not brought bankruptcy to states or employers. They have brought the kind of support to the unemployed that was envisioned by Congress when it passed the Social Security Act of 1935.

Those who are concerned with the rights of the unemployed must press for the amendment of section 597.4. If amendment proves impossible, the courts must restrain the reach of the statute against good faith recipients. New York must realize that preservation of systemic solvency can be achieved through better administration and funding, not through the manipulation of claimants as a safety net for an ineffective bureaucracy. It is only through vigorous advocacy that New York — and many other states — will develop a truly fair unemployment insurance system.

PATRICK M. MULDOWNNEY*

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