

Introduction to State Unemployment Insurance Trust Fund Solvency

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State UI Solvency Outline

- Background/Historical Overview
- Current Status of Funds
- Factors behind Low Solvency
- Options for Financing
- Options for States to Address

UI Program Goals

Established in 1935 as a Federal-State program:

- To help stabilize the workforce by providing temporary income support to individuals who are involuntary unemployed.
- Provide economic stimulus to the economy during recessionary periods.

Unemployment Insurance Program Financing

Employers

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graph TD; A[Employers] --> B["1) Federal Tax"]; A --> C["2) State Tax"];
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1) *Federal Tax*

Flat Rate:

0.8% on first \$7,000 of wages
(\$56 per covered employee.)

Pays for:

- Administration- UI / ES
- Federal Unemployment Account (FUA)
- Employment Security Administration Account (ESSA)
- Emergency Unemployment Compensation Account (EUCA)

2) *State Tax*

Experience Rated:

Taxable Wage Rate
Tax Schedule

Pays for:

State benefits

State Regular UI Programs (2009)

	Low	Average	High
<u>Benefits</u>			
Proportion of Wages Replaced by UI ¹	24% (PR)	36%	56% (HI)
Proportion of Unemployed Receiving UI ² ...	26% (SD)	42%	64% (PA)
Average Duration.....	13 wks (NE)	17 wks.	20 wks (DE)
Average Weekly Benefit Amount.....	\$194(MS) ³	\$309	\$391(WA)
<u>Taxes</u>			
Taxable Wage Base	\$7,000 (8 states)	\$10,250 (median)	\$35,700(WA)
Cost Per Employee ⁴		\$293 (Average)	

¹ Proportion of the average weekly benefit to the average weekly wage of all covered employment.

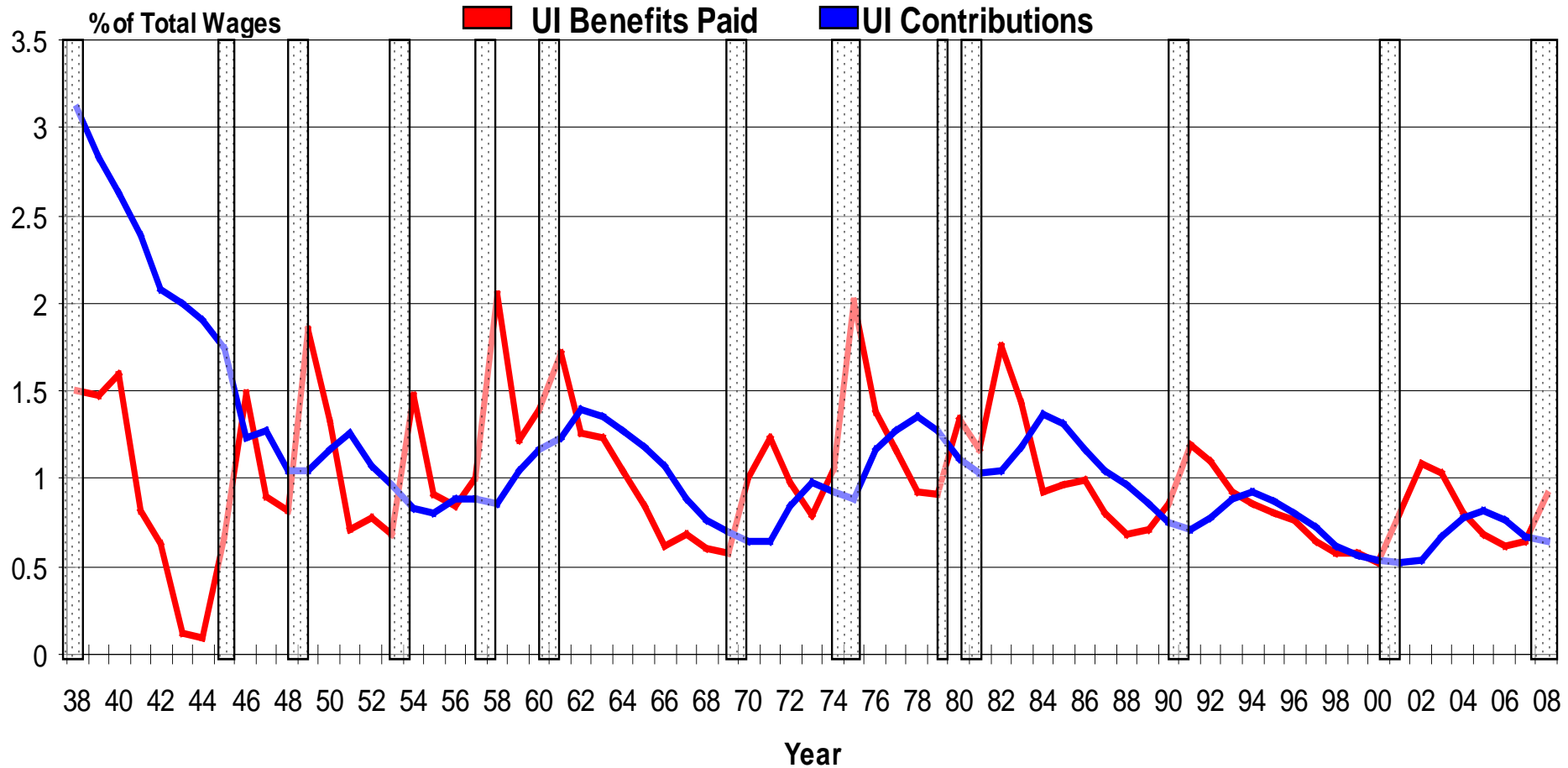
² Proportion of those claiming UI in the regular state program to total unemployment

³ Including all non-states, Puerto Rico is the lowest at \$114.

⁴ Cost per employee is measured as total UI contributions divided by total covered employment

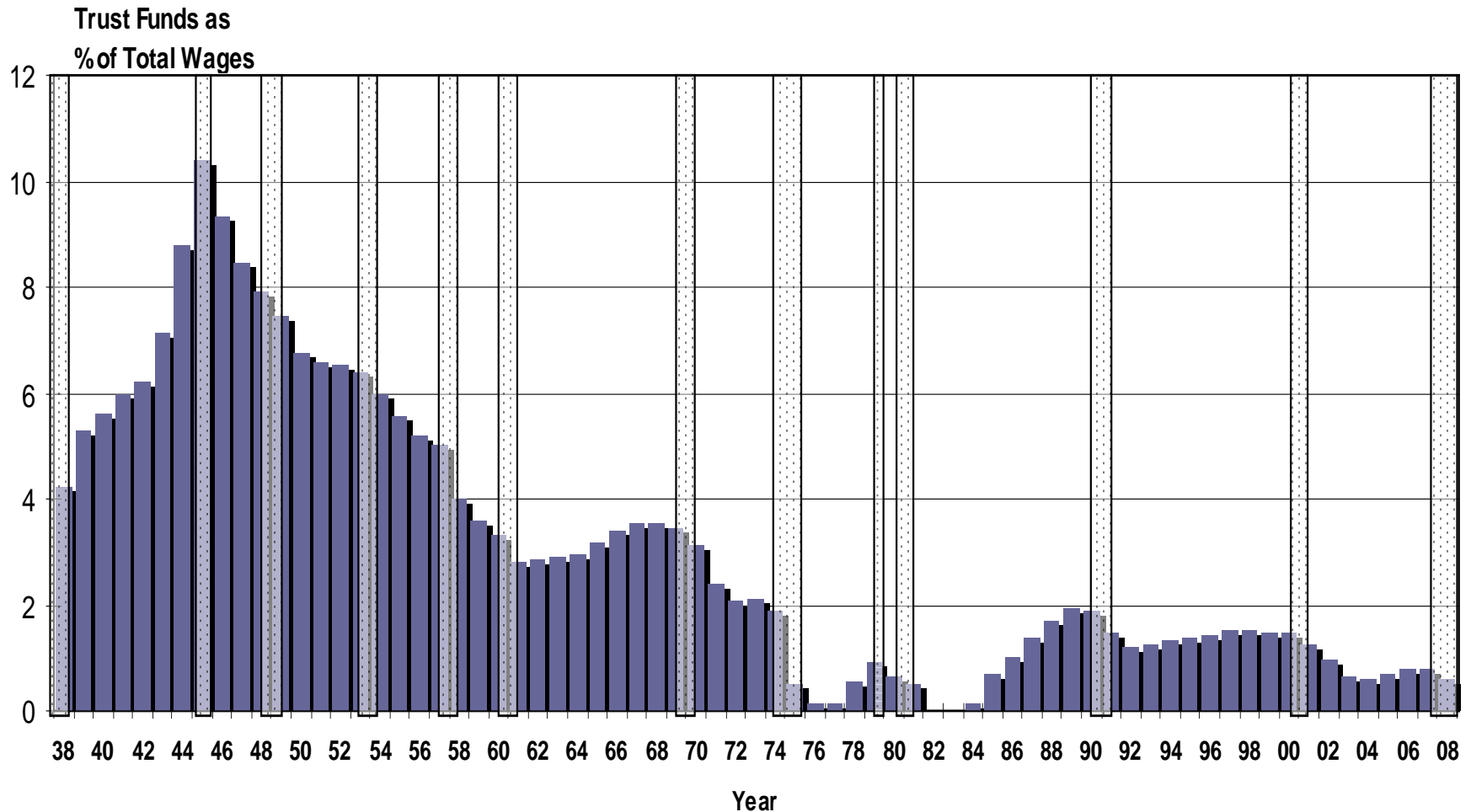
History of UI Financing

UI Aggregate Benefits and Contributions as % of Total Wages

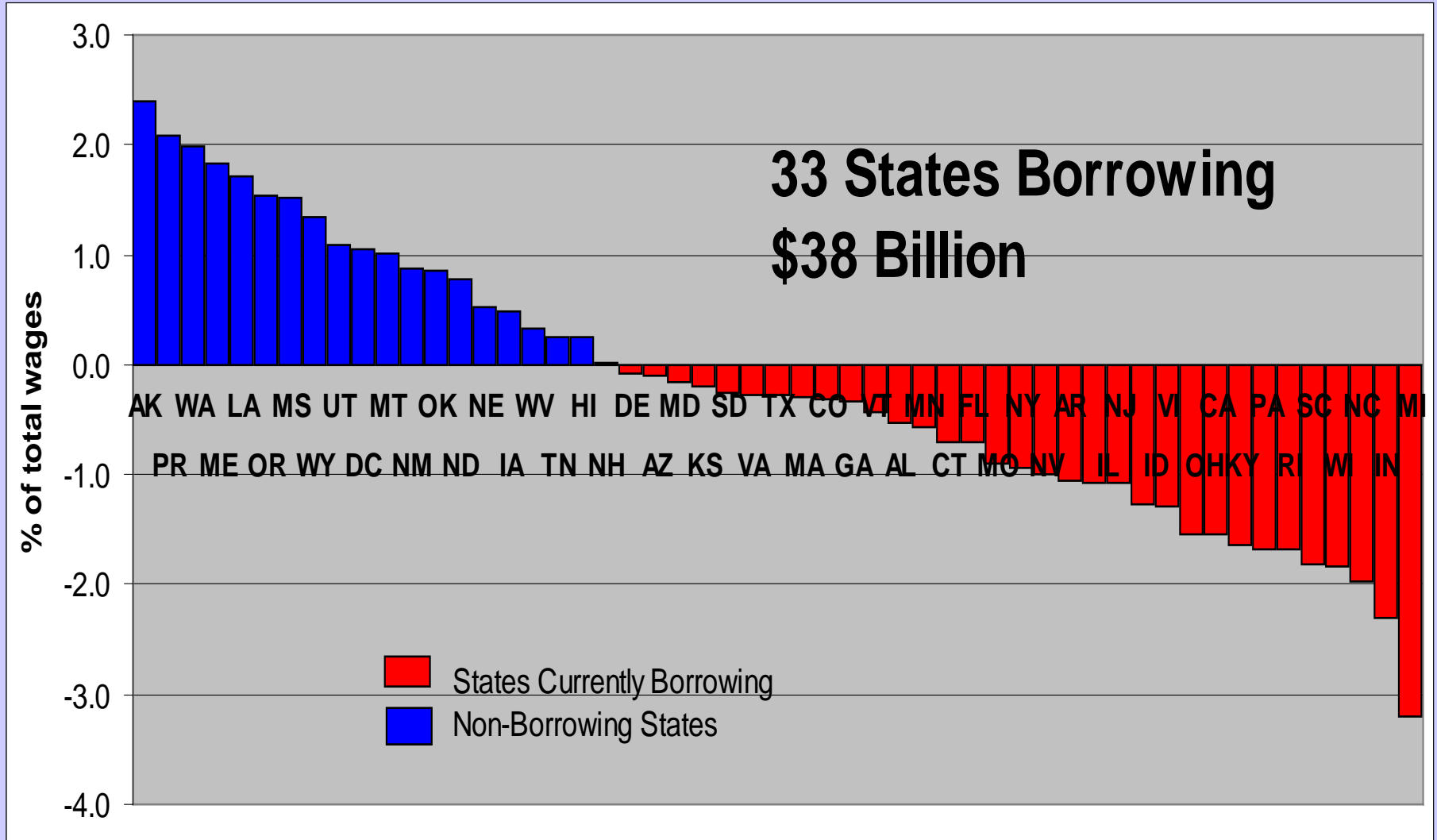


History of UI Financing

Aggregate State Trust Fund Reserves



UI Trust Fund Balances and Loans as a % of Total Wages (May 31, 2010)



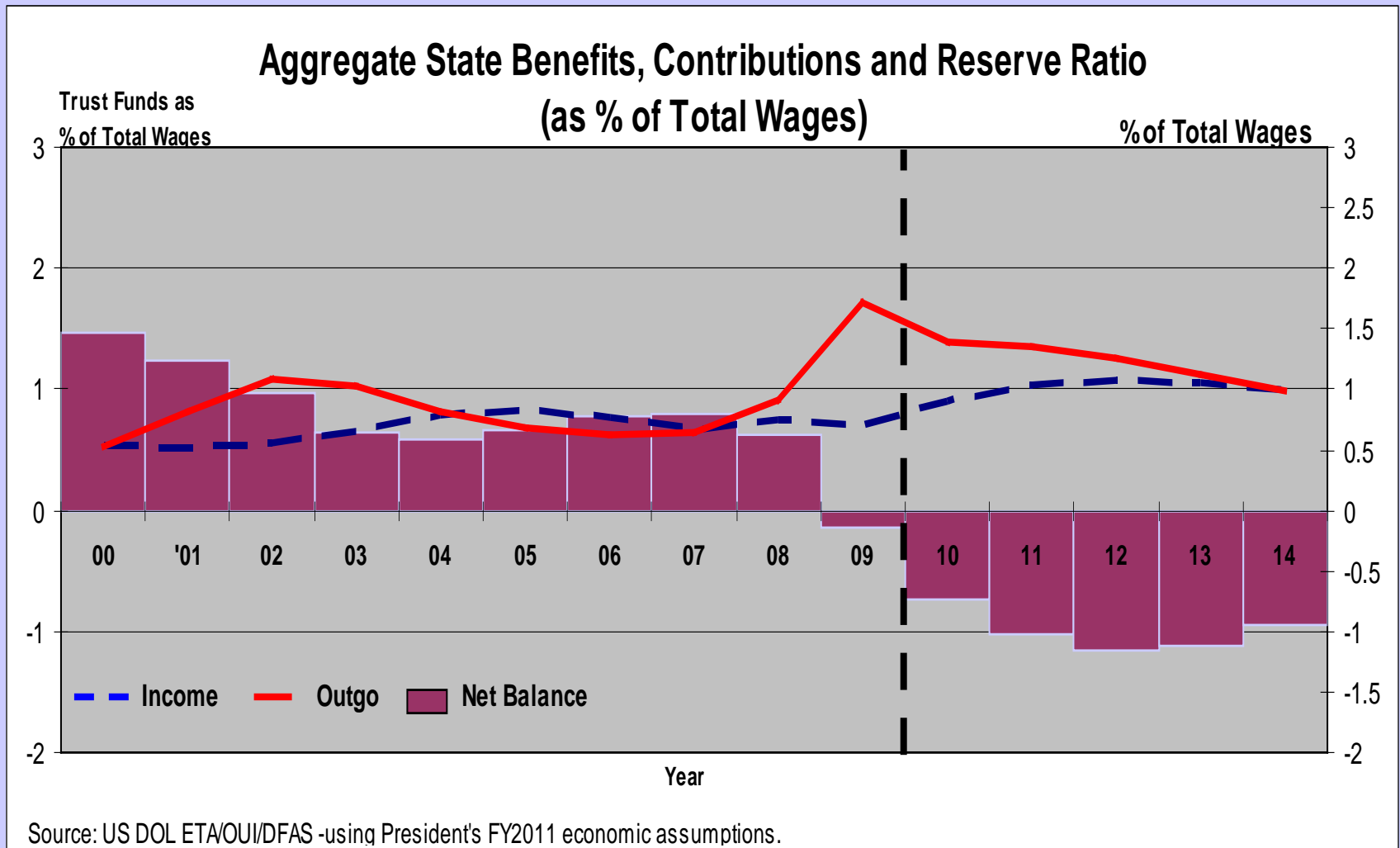
AVERAGE HIGH COST MULTIPLE

$$\text{AHCM} = \frac{\frac{\text{TF Balance (as of 12/31)}}{\text{Covered Wages (calendar year)}}}{\frac{\text{Benefits Paid for a calendar year}}{\text{Covered Wages for the same calendar year}}}$$

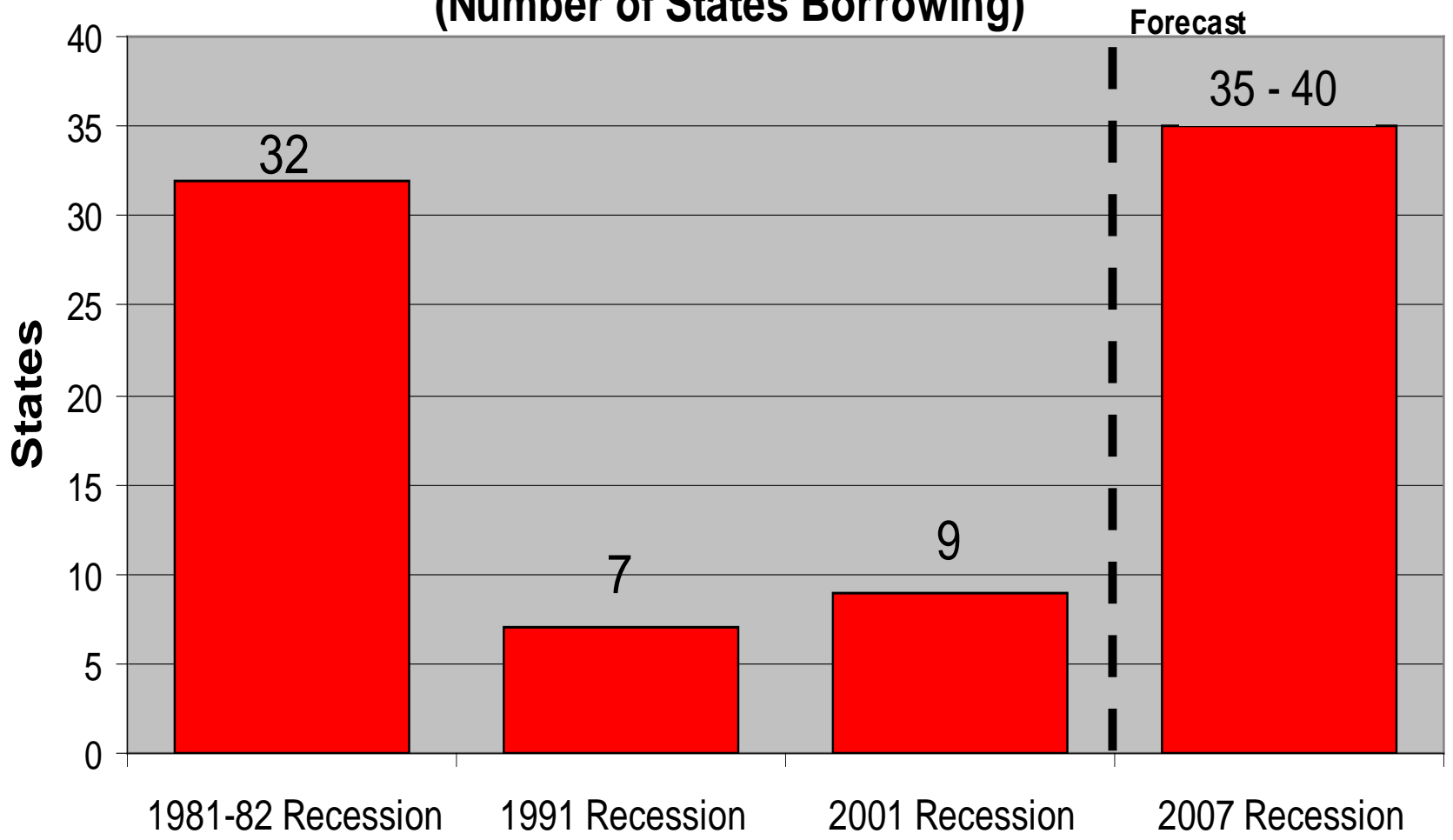
Average of 3 highest yrs over the last 20 yrs, or last 3 recessions, whichever is longer

The AHCM represents the number of years a state can pay out benefits if it paid at the rate it paid during the three highest years over the previous 20 (or over the last 3 recessions, whichever is longer) without receiving any additional revenue.

Current Status and Projection of State UI Trust Funds



Historical and Forecasted Level of Title XII Borrowing (Number of States Borrowing)

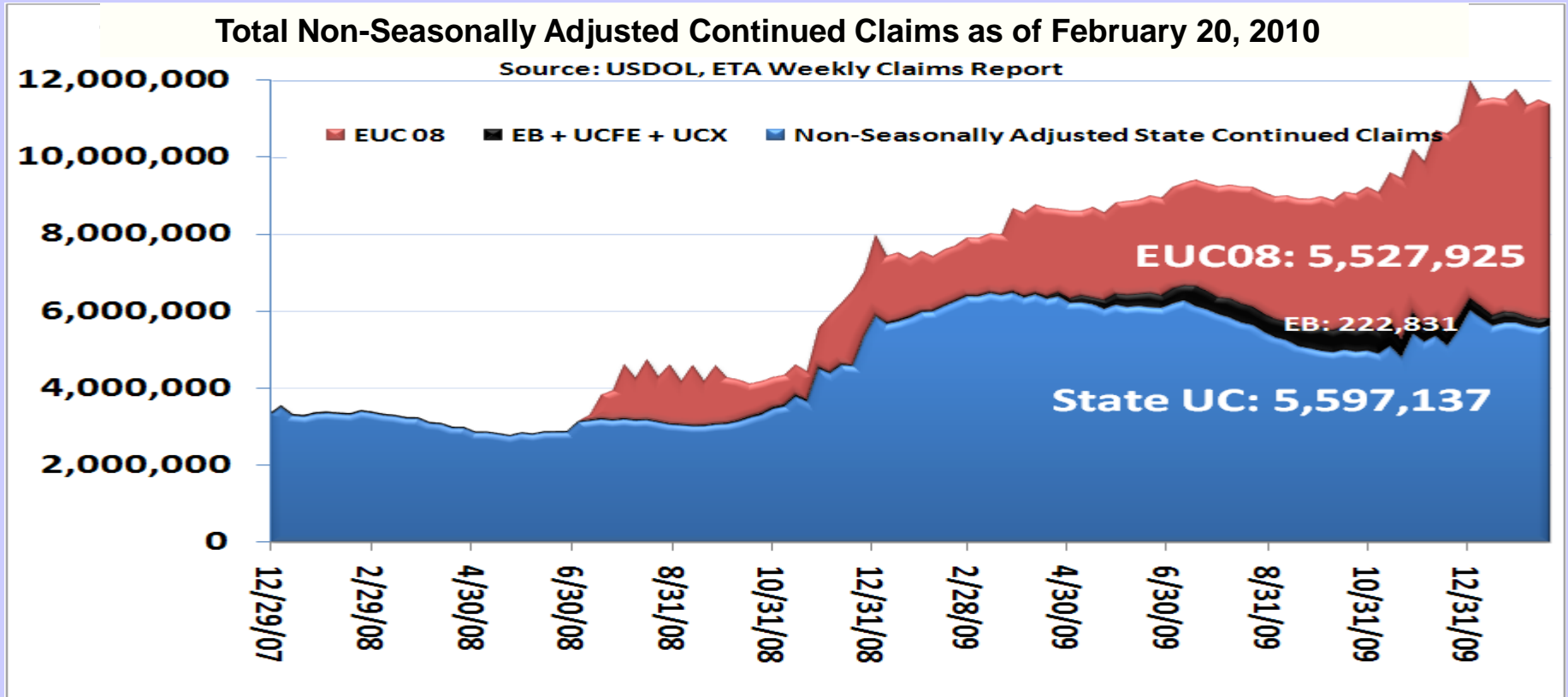


* Forecast Based on President's FY2011 economic projections

Source: U.S. Dept. of Labor, Office of Unemployment Insurance, Division of Fiscal and Actuarial Services

Factors Behind Low Solvency Levels

1) High Unemployment Recession



Cal. Year	UI Benefit Amounts	Beneficiaries
	State program	State program
2007	\$31 Billion	7.6 million
2008	\$41 Billion	10.0 million
2009	\$80 Billion	14.4 million

Factors Behind Low Solvency Levels

2) Inadequate Financing of State UI Benefits

a) Legislated Cuts in State UI Tax rates

29 States passing legislation with at least a 20% reduction in UI Tax Rates in one year (1995-2005).

Factors Behind Low Solvency Levels

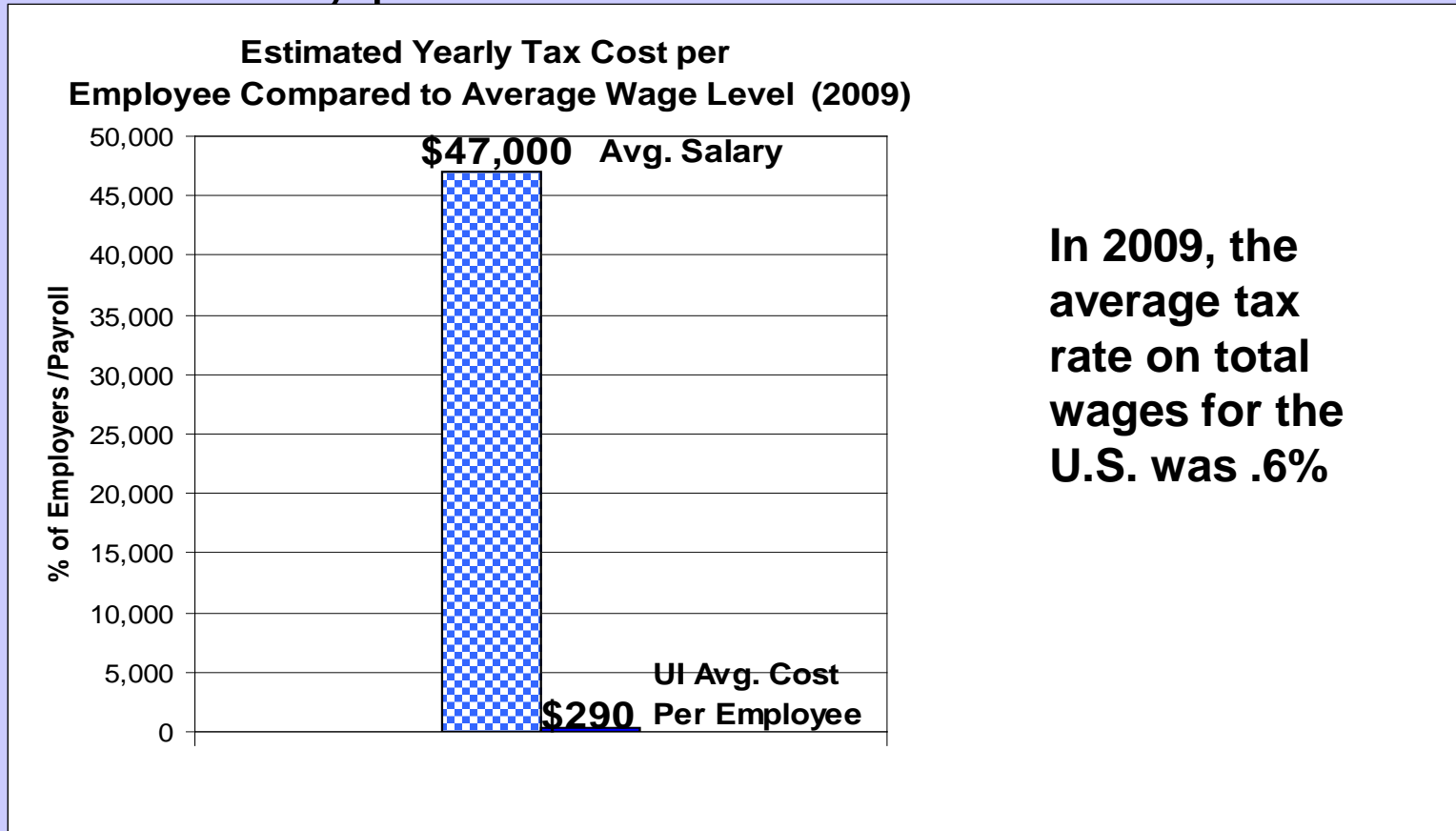
b) Deterioration in Proportion of Wages that are Taxed for Unemployment Insurance

In 2007 29 States had wage bases at \$10,000 or below - including 9 with the minimum allowable wage base of \$7,000.

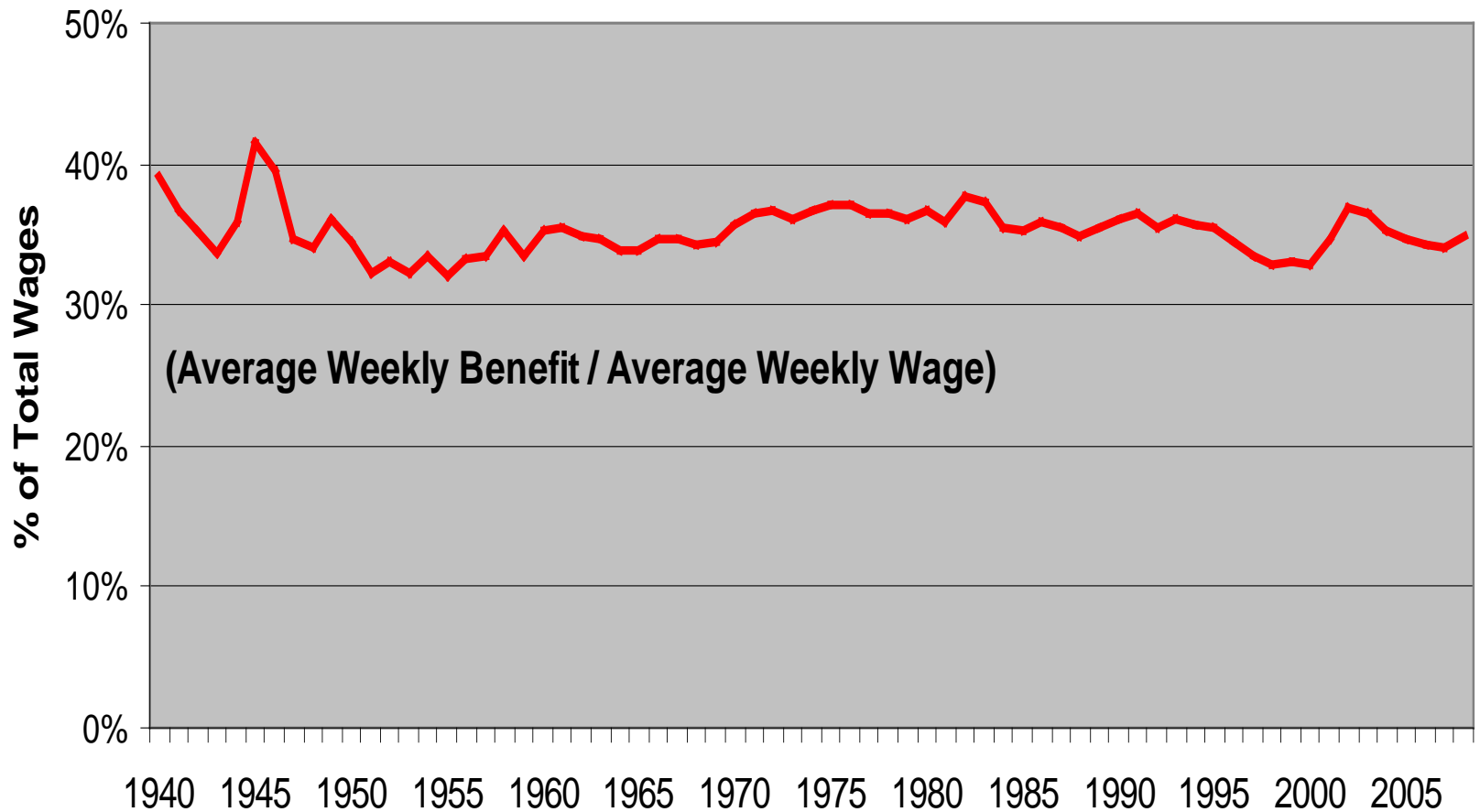


UI Tax Burden

Overall, average State tax rates were declining for two years leading up to the recession, even though State trust fund levels were at historically low levels for a pre-recessionary period.



Replacement Ratio (1940-2008)

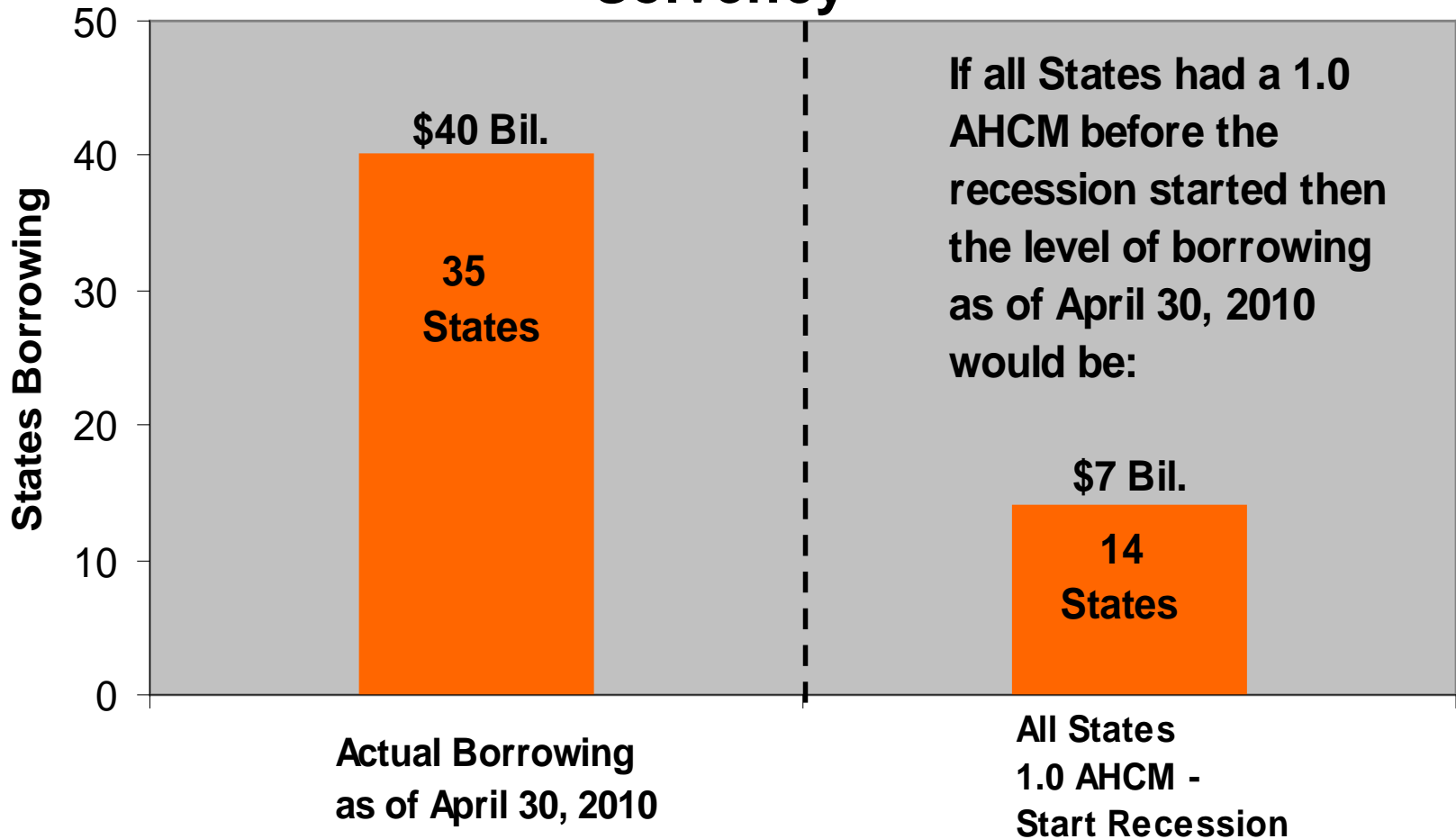


(Average Weekly Benefit / Average Weekly Wage)

Replacement Ratio is measured as the U.S. average weekly benefit of all claimants divided by the average weekly wage in covered employment.

Impact of Low Solvency

Amount of Borrowing Due to Low Solvency

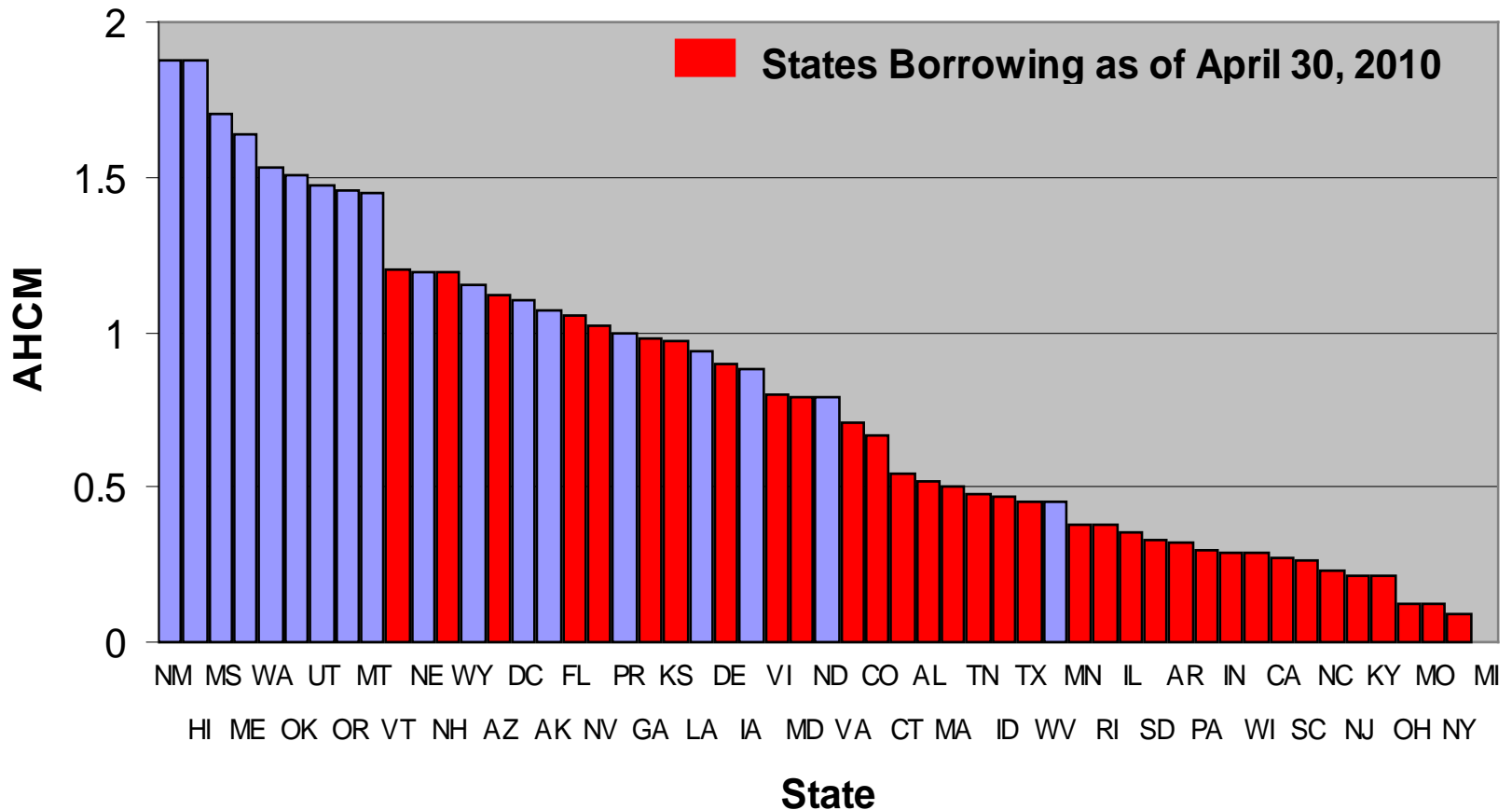


Financing Options

- **Deficit Financing** – A State uses borrowed funds to pay for UI benefits.
- **Forward Funding** – A State builds up its trust fund reserve in anticipation of increased outlays.
- **Pay–As–You–Go Financing** – a State taxes at a rate equal to the amount of benefits paid, (reimbursement system).

Solvency Level Before Recession

Average High Cost Multiple (12/31/2007)



Why Forward Funding

1) Forward Funding increases the effectiveness of UI as an automatic stabilizer for the economy

In a recession, by automatically directing more money towards people with high spending patterns, UI helps reduce the loss in GDP and reduce unemployment.

Latest study shows that the UI program during recessions mitigated the loss in GDP by approximately 15% and saved on average 131,000 jobs annually. (Coffey, 1999)

Why Forward Funding

2) **Helps avoid UI benefit cuts**

Historically a low or insolvent trust fund has led some states to cut benefits at the worst times.

Six states have a provision that lowers the maximum weekly benefit when the trust fund falls.

Three of the nine states that borrowed funds following the 2001 recession cut benefits.



Why Forward Funding

3) Helps Avoid tax increases when employers are most vulnerable.

With forward funding, during a recession a State is able to rely on a cushion of funding to pay benefits, without having to increase taxes at the worst time.

Also, a State trust fund can quickly deteriorate when large firms go bankrupt and leave large social costs on the remaining firms, which then requires tax increases at the worst time.

Legislative Response to 80's Recession

Federal Law Changes

- Federal Wage Base increased from \$6,000 to \$7,000
- FUTA tax rate went from .7% to .8%
- Requirement for the minimum maximum tax rate went from 2.7% to 5.4% (five yr. phase in)
- Charging of interest on loans – w/ flexibility for repayment
- Raised Individual State EB triggers – under IUR (no TUR option)
- Repealed national EB Triggers

Legislative Response to 80's Recession

State Law Changes

- 14 States legislatively increased their wage bases by at least ten percent - 1982 to 1985.
- Tightening of benefit receipt in a number of states. The U.S. reciprocity rate fell from a high of 44% in 1980 to 29% in 1984.
- The U.S Replacement rate fell every year from 1980 to 1988 from 37% down to 35%.

Current Solvency Legislation

Federal Law Changes

Currently States are able to borrow interest-free from Jan. through Sept. if re-payment is made by Sept. 30 and no further borrowing is made, (without American Recovery and Reinvestment Act of 2009).

Proposed New Regulation Requirement for Interest Free Loans:

States must have achieved a level of solvency (1.0 AHCM) in one of the prior five years and then not reduce tax rates below a specified level, in order to be eligible for the interest free period.

Current Solvency Legislation

State UI Law Changes

Enacted

West Virginia: Increased wage base from \$8,000 to \$12,000 in 2009.

Tennessee: Increased wage base from \$7,000 to \$9,000 in 2009.

Vermont: Increased wage base from \$8,000 to \$12,000 in 2010.

South Dakota: Emergency Surtax of 1.5% on taxable wages in 2010.

New Hampshire: Increased wage base from \$8,000 to \$10,000 in 2010,
(2011 will be \$12,000, and 2012 will be \$14,000).

Repayment of Loans

Title XII Federal Credit Reduction Offsets

After a state has passed two January 1's with an outstanding loan in each successive year it will begin to lose a portion of its credit which will go towards repayment of the loan:

Years > Loan	FUTA CREDIT Reduction	Additional Amount	Total FUTA Tax Rate
1	0.0%	0.0%	0.8%
2	0.3	0.0	1.1
3	0.6	2.7 Add-on	1.4 or more
4	0.9	2.7 Add-on	1.7 or more
.	.	.	.
19	5.4		6.2

Estimated Federal Tax Rate Increases to Repay Advances

State	Advances as of 4/30/2010 Balance (\$M)	Estimated FUTA Credit Reduction*			
		2009 (%)	2010 (%)	2011 (%)	2012 (%)
Alabama	283.0			0.3	0.6
Arkansas	330.9				0.3
Arizona	24.9			0.3	0.6
California	8,873.1			0.3	0.6
Colorado	253.7				0.3
Connecticut	498.5			0.3	0.6
Delaware	12.9				0.3
Florida	1,612.5			0.3	0.6
Georgia	416.0			0.3	0.6
Idaho	202.4			0.3	0.6
Illinois	2,239.6			0.3	0.6
Indiana	1,837.3		0.3	0.6	0.9
Kansas	88.2				0.3
Kentucky	795.1			0.3	0.6
Massachusetts	387.3				0.3
Maryland	133.8				0.3
Michigan	3,876.8	0.3	0.6	0.9	1.2
Minnesota	490.0			0.3	0.6
Missouri	722.1			0.3	0.6
North Carolina	2,276.1			0.3	0.6
New Hampshire	19.4				0.3
New Jersey	1,749.6			0.3	0.6
Nevada	395.4			0.3	0.6
New York	3,176.9			0.3	0.6
Ohio	2,314.2			0.3	0.6
Pennsylvania	3,008.6			0.3	0.6
Rhode Island	222.7			0.3	0.6
South Carolina	886.7		0.3	0.6	0.9
South Dakota	24.0			0.3	0.6
Tennessee	20.7				0.3
Texas	1,030.8			0.3	0.6
Virginia	346.9				0.3
Virgin Islands	13.3			0.3	0.6
Vermont	32.7			0.3	0.6
Wisconsin	1,424.8			0.3	0.6
Total	40,020.7				

* Assumes balance on January 1 every year and on November 10 of the indicated year and no application of the possible third year 2.7% add-on amount.

Options to Address Under-Funding of State UI Benefits

Federal

Raise Federal Wage Base
(1983)

Greater Federal Financing
(ARRA,2009)

Solvency Standards/Incentives
(ACUC,1996)

Re-Insurance (NCUC,1980)

State

Raise Tax Adequacy
(Wage Base/ Range of Rates)

Reduce Overpayments

Improve Re-employment Serv.

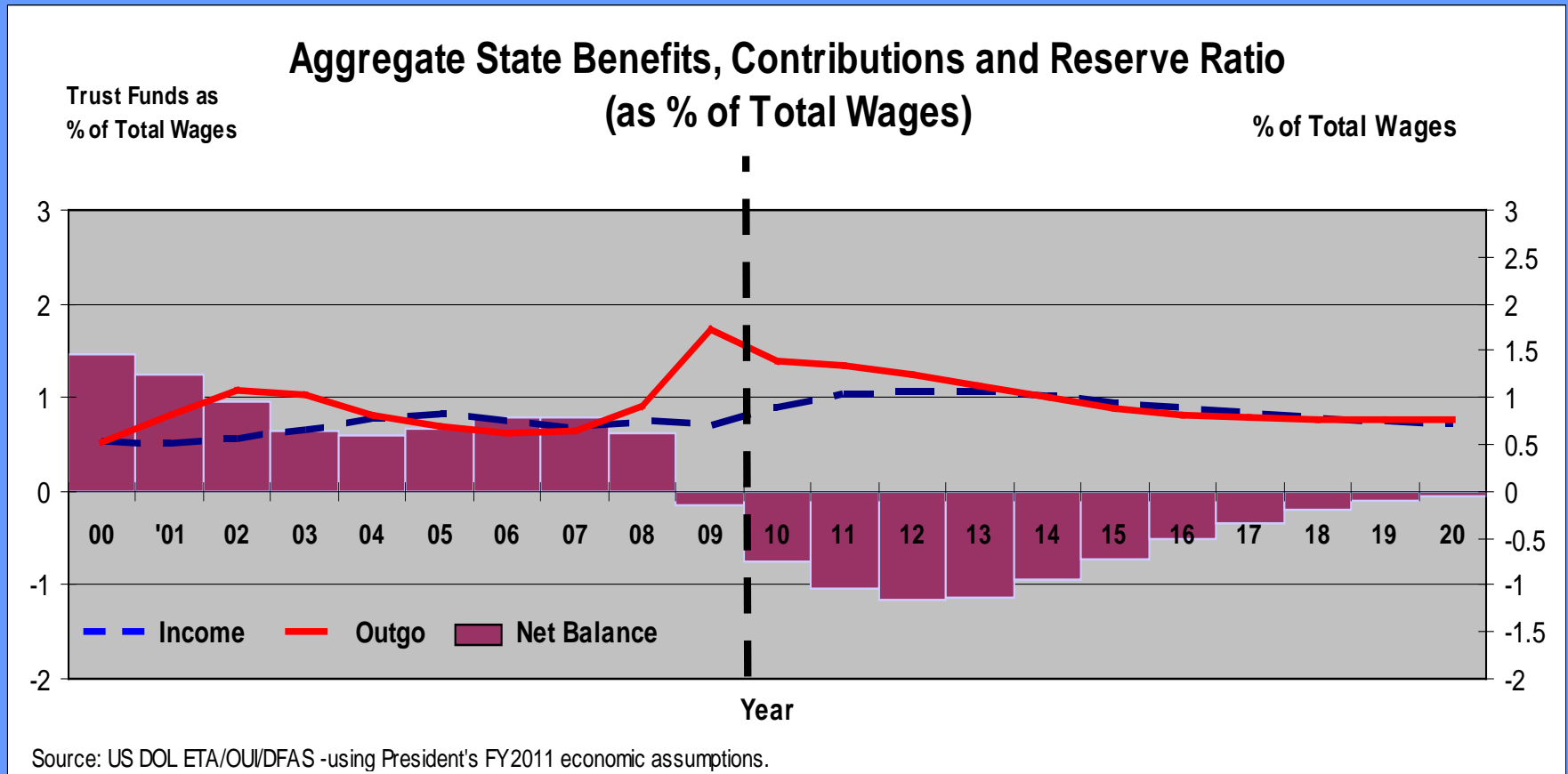
Private Financing of UI Debt

Employee Tax

Summary

- Combination of historically high unemployment levels and the cutting of UI taxes has created a crisis in the financing of State UI programs.
- This crisis endangers the valuable role that a forward funded UI program plays in the economy.
- A rich body of available options including varied State experiences exists for confronting this situation.

Long Term Forecast with No Solvency Changes



❖ **Aggregate reserves close to zero by 2020**

Resources Available to States

- Technical assistance available on:
 - Solvency
 - Profiling
 - Overpayments
 - Reemployment
 - UI Modernization legislation

Information

- Overview of UI:

<http://www.ows.doleta.gov/unemploy/pdf/partnership.pdf>

- Comparison of State UI Laws:

<http://www.ows.doleta.gov/unemploy/statelaws.asp>

- Weekly Claims:

http://www.ows.doleta.gov/unemploy/claims_arch.asp

- Summary of EUC:

<http://www.ows.doleta.gov/unemploy/pdf/euc08.pdf>

Information

- UI Data Summary:

<http://www.ows.doleta.gov/unemploy/content/data.asp>

- State Loan Balances:

http://www.treasurydirect.gov/govt/reports/tfmp/tfmp_advactivitiessched.htm

- Total Unemployment Rate:

<http://www.bls.gov/>

UI Outlook & other Program Statistics:

- <http://www.ows.doleta.gov/unemploy/finance.asp>
- **Periodic Data Available**
 - [Annual Program and Financial Data \(ET Financial Handbook 394\)](#)
 - [Quarterly Program and Financial Data \(Data Summary\)](#)
 - [Monthly Program and Financial Data](#)
 - [Weekly Claims Data](#)
 - [Characteristics of the Insured Unemployed](#)
 - [**Significant Measures of State UI Tax Systems**](#)
 - [Average Employer Contribution Rates by State](#)
 - [Program Charts, Graphs, and Tables](#)
 - [Estimated FUTA Receipts vs. Amounts Returned](#)

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Questions