Trust Fund Loans: Interest Charges and Credit Reductions

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Topics

- Current and projected Title XII loans
- Interest on loans
- FUTA credit reductions
AHCM By State Pre-Recession

States Above 1.0 AHCM

State Benefits -- % of Wages
Title XII, Social Security Act (SSA)

- Provides for advances (loans) to states from the Federal Unemployment Account (FUA)
- States make loan requests to USDOL
- States draw from FUA as needed
Number of States that have Borrowed: 36

Peak Amount of Loans: $48.5 Billion

Number of States with Current Loan Balance: 28

Current Loan Balance: $38.1 Billion
Projected Loan Balances

End of Federal Fiscal Year

Billions $

Actual

Forecast

Interest Payments
1202(b), SSA, 20 CFR Part 606

• Interest accrues **daily** on advances on a federal fiscal year basis

• Interest rate changes each calendar year – equal to rate earned by UTF Oct.-Dec.

• Interest is generally due and payable no later than Sep. 30

• Interest cannot be paid directly or indirectly from funds in the state’s unemployment fund – 3304(a)17 FUTA

• Reed Act funds cannot be used to pay interest as they reside in the fund
A state borrows $10 million on 11/1/2011 and repays $10 million on 5/15/2012

Oct-Dec 2011 Interest = $10 M x 61 days x 4.09% / 365
= $68,353

Jan-Sep 2012 Interest = $10 M x 136 days x 3.0% / 365
= $111,781

Total Interest Due 9/30/2012 = $180,134
Interest Payments
3304(a)(17), FUTA and 303(c)(3), SSA

• Paying interest on time is a requirement to be certified under the FUTA for employer tax credits
• Paying interest on time is a requirement to be certified under the SSA for administrative grants
Cash Flow Loan Example

State Begins to Receive Advances

State Repays Advances

Contributions
Benefits
Cash Flow Loans

• No interest will be assessed on loans received Jan.–Sep. if:
  – The loans are repaid by Sep. 30;
  – No other loans are taken out between Oct. 1 and Dec. 31; and
  – The state meets the funding goals specified in regulation *(20 CFR 606.32)*

• Starts 2014
Cash Flow Loans

- If a state borrows between Oct. 1 and Dec. 31, the interest that would have been due Sep. 30 must be paid in full the day after the new loan.
Funding Goals

• Starting in 2014, a state must meet the following criteria to get a cash flow loan:
  – Have had an Average High Cost Multiple (AHCM) meeting the specified target within the past 5 years
  – For each year between the year in which the solvency target was last met and the year of the loan, the state’s average tax rate must be at least 80 percent of the prior year’s average tax rate and at least 75 percent of the state’s five-year average benefit-cost ratio.
Phasing In of AHCM Criterion

• For calendar years 2014 through 2018 the AHCM criterion will be phased in as follows:
  – 2014 AHCM of 0.50
  – 2015 AHCM of 0.60
  – 2016 AHCM of 0.70
  – 2017 AHCM of 0.80
  – 2018 AHCM of 0.90

• Beginning in 2019 the AHCM required to meet the solvency criterion is 1.0
May to September Delay

- A state may delay payment of interest accrued on new loans in May through September until Dec. 31 of the following calendar year
  - State must pay interest due on loans taken before May 1 by September 30
  - Interest continues to accrue on the deferred interest
High TUR Delay

- State may delay interest payment for nine months after Sep. 30 if its TUR averaged 13.5% for the 12 months ending August.
  - Interest does not continue to accrue during the delay period
High IUR Deferral

- State may defer interest payments if its IUR averaged 7.5% for the first six months of the previous calendar year.
  - State pays one-fourth of interest due on Sep. 30, then one-fourth each of the next 3 years
  - No interest accrues during the deferral period
Interest Payments -- 2011

• Interest due 9/30/11
• 29 states paid $1.2 billion
• NV had a 9-month high unemployment deferral
• CO had a partial deferral for May-Sep loans
• 7 states had cash-flow loans for 2011
• One state paid late and lost some administrative funds
Voluntary Repayments

- States are not required to repay advances, but repayments are made in two ways.
- State may make voluntary repayments at any time.
- Voluntary repayments are applied on a last made first repaid basis \((UIPL\ 22-02)\).
The second method of loan repayment is via FUTA credit reduction.

If a state has a loan balance on January 1 of two consecutive years and has not fully repaid all loans by November 10 of the second year, employers may be subject to reduction in their FUTA credit.

The credit reductions generally increase the effective FUTA rate by 0.3% each year the balance remains unpaid.

Receipts credited against the loan balance.
## FUTA Credit Reduction

<table>
<thead>
<tr>
<th>Years After First Loan(^1)</th>
<th>Basic Credit Reduction</th>
<th>Additional Credit Reduction</th>
<th>Total FUTA Rate(^2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.6%</td>
</tr>
<tr>
<td>2</td>
<td>0.3%</td>
<td>0.0%</td>
<td>0.9%</td>
</tr>
<tr>
<td>3</td>
<td>0.6%</td>
<td>2.7 Add-on</td>
<td>1.2% or more</td>
</tr>
<tr>
<td>4</td>
<td>0.9%</td>
<td>2.7 Add-on</td>
<td>1.5% or more</td>
</tr>
<tr>
<td>5</td>
<td>1.2%</td>
<td>BCR Add-on(^3)</td>
<td>1.8% or more</td>
</tr>
</tbody>
</table>

\* \* \* \*

| 19                           | 5.4%                   | BCR Add-on                 | 6.0%                   |

\(\text{1 In terms of consecutive January 1st with an outstanding balance}\)

\(\text{2 FUTA rate with full 5.4% credit was 0.8% through June 2011 and is currently 0.6%}\)

\(\text{3 If BCR Add-on is waived, 2.7 Add-on applies.}\)
2.7 Add-on
3302(c)(2)(B), FUTA

Compute \( X = (2.7\% \times (7,000/\text{U.S. Avg. Annual Wage})) \)

If State ATRtot < X,

\[
\text{Add-on} = (X - \text{ATRtot}) \times (\text{State Avg. Ann. Wage}/7000)
\]

Example (2012 estimate):

\[
X = (2.7\% \times 7,000 / 50,003) = 0.38\%
\]

State ATRtot = 0.3%

\[
\text{Add-on} = (0.42\% - 0.3\%) \times (36,533/7,000) = 0.63\%
\]
BCR Add-on
3302(c)(2)(C), FUTA

BCR Add-on = (higher of BCR or 2.7%) – ATR

- BCR is the 5-year average benefit cost rate

- ATR is the average tax rate on taxable wages

- May be waived if no action taken to reduce solvency
Avoidance of FUTA Credit Reduction
3302(g), FUTA

- A state may avoid credit reduction for a year by:
  - Repaying any advances received during the one-year period ending Nov. 9 of that year;
  - Repaying an additional amount equal to the amount employers would pay through credit reductions;
  - Taking action to increase solvency by the amount of the potential credit reduction; and
  - Not borrowing from Nov. 1 of the tax year through Jan. 31 the following year.
FUTA Credit Reduction Cap
3302(f), FUTA

• Beginning with the 2nd year a state faces credit reduction, states may have the reduction capped if these criteria are met:
  – No action taken during 12 months ending September to reduce tax effort;
  – No action taken to reduce solvency;
  – State’s average tax rate on total wages exceeds 5-year benefit cost rate on total wages; and
  – Loan balance not greater than balance 3 years earlier.

• A state that qualifies for a cap will have its credit reduction set at the greater of 0.6% or the prior year’s level

• If the state qualifies for a cap, that year is not counted in the number of consecutive January 1sts
FUTA Credit Reductions -- 2011

• 21 states have a credit reduction for 2011
• MI has a 0.9% reduction, IN 0.6%, the rest 0.3%
• SC qualified for avoidance
• Up to 30 states in 2012