

Albany's Chance: Restoring the Solvency and Stability of the Unemployment Insurance Trust Fund¹

Executive Summary

Before the start of this decade, most New Yorkers never thought twice about unemployment insurance. Back then, New Yorkers affected by the post 9-11 recession or today's protracted slump could not have foreseen the long unemployment spells waiting right around the corner or known that they would depend on a weekly benefit check to forestall foreclosure. And, these workers cannot be blamed for being disappointed with the glaring weaknesses facing New York's unemployment insurance system—weekly benefits that trail all our Northeast neighbors and even Kansas and Arkansas, and an unemployment trust fund that must borrow billions from the federal government to keep the system afloat.

Over the past two decades, our fiscal and economic stewards in Albany made poor decisions regarding the state's unemployment insurance trust fund, the consequences of which are now coming to fruition in the form of unprecedented borrowing and impending federal penalties on employers.

When the economy was strong during the 1990s and over much of the past decade, New York had the opportunity to accumulate unemployment insurance trust fund reserves by adjusting the state's taxable wage base (i.e., the amount of wages subject to taxation) upward. Had New York been more proactive, the state would not be \$3.2 billion in debt to the U.S. Treasury and could afford to pay unemployment insurance benefits that reflect the true cost of living throughout the state.

New York's unemployment insurance trust fund will eventually have to pay back its debt to the federal government, but it is up to Albany to decide the terms of that repayment. If the state fails to act, the federal government will begin penalizing employers by raising the annual federal tax by \$21 per employee in 2012 until federal loans are repaid, a process that is expected to take through 2018 and cost employers \$1.3 billion in interest payments and \$5 billion in federal tax penalties. In the end, the fund will be as susceptible to future recessions as it is today.

Or, Albany can choose its own terms by passing unemployment insurance reform legislation. Two active bills (S. 2245B/A. 4921A and S. 8423/A. 11607) would put the state on the right track toward solvency by gradually increasing the state's taxable wage base to account for economic growth and the weekly

benefit amount to keep pace with the cost of living. While both proposals would bring the fund back to solvency, this report focuses on the Governor's proposal (S.8423/A.11607), which has a better chance of garnering enough support to be enacted. Under the Governor's proposal, the state trust fund will become solvent in 2015, saving the state's employers \$700 million on interest payments. More importantly, the fund will be on firmer footing by 2018 with reserves of \$1.5 billion.

The remainder of this report explains the basics of unemployment insurance financings as well as how New York's trust fund came to be so far in debt, despite paying comparatively low benefits to jobless workers. It concludes with a cost comparison between the baseline scenario (i.e., doing nothing) and proposed legislation.

Unemployment Insurance Keeps New York's Jobless Workers Afloat

The current recession has shown New Yorkers the critical value of a strong unemployment insurance program. Over the past year, as many as 1 million New York workers and their families have counted on state unemployment insurance (UI) benefits at some point to put food on the table and keep the lights on.² And since the start of the recession, federal and state UI benefits pumped \$16.6 billion into the state's economy, counteracting billions of dollars in lost consumer spending due to the downturn.

Today's slow recovery means that the state will need a strong UI program over the next several years. Although New York's unemployment rate is starting to improve, and the state has recently seen positive job growth, unemployment will remain a long-term problem. The state added about 18,000 jobs per month for the first five months of 2010 before losing 22,500 in June. Despite this early growth, the state still has an unemployed population of nearly 800,000 people and compared to the start of the recession, the state is short 248,000 jobs. Thus, the unemployment benefit program is still playing a key role in the state—with the state paying 493,000 federal and state UI claims a week in June, compared to just 190,000 per week when the recession began in 2007.

Unemployment Insurance is a Key to Economic Recovery

The continued viability of the unemployment safety net and its capacity to support New York's economy depends on an effective mechanism for financing benefits. State unemployment insurance benefits are paid out of a dedicated UI trust fund (UITF) that is made up of unemployment insurance payroll taxes deposited by employers on workers' behalf.

In addition to supporting individual families, the other purpose of the unemployment program is to help stabilize the state's economy during downturns. For the UI system to function properly, an adequate unemployment insurance trust fund is critical. Wayne Vroman, the nation's leading authority on UI financing, summarizes the overall economic theory supporting forward funding of UI programs:

Trust fund balances are built up before recessions, drawn on during recessions, and then rebuilt during the subsequent recoveries. The funding arrangement implies that the program acts as an

automatic stabilizer of economic activity, that it makes larger benefit payments than tax withdrawals during recessions and larger tax withdrawals than benefit payments during economic expansions.³

State UI programs are more effective counter-cyclical mechanisms when adequate benefits are paid out of accumulated trust fund reserves during downturns, without the need to rely on tax increases or benefit cuts to remain solvent. The contrasting approach to UI financing—sometimes termed “pay as you go”—keeps UI payroll taxes and trust fund levels as low as possible when the economy is strong and then raises taxes and cuts benefits due to financial stress during recessions. This approach turns the UI program on its head, completely undermining its role of providing economic stimulus. Encouraging forward funding of the state UI trust fund is essential if our UI program is going to serve as a more effective economic stabilizer in future recessions.

Today’s Trust Fund Crisis was Years in the Making

Albany has not fulfilled its role as steward of the unemployment program’s finances, despite ample warning before the start of this recession.

The 1994 federal Advisory Commission on Unemployment Compensation made recommendations that defined forward financing goals. The most important measure compares the size of trust fund reserves to past benefit payouts during recessions. Termed a “cost multiple,” this measure of solvency uses past performance to assess the adequacy of current reserves by comparing trust fund reserves to historically high UI benefit payment levels during prior recessions. The resulting multiple is calculated in such a way that 1.0 is equal to one year of reserves at historic levels of high benefit payments: this measure was recommended by the Advisory Commission and other UI financing experts as the appropriate level of pre-recession reserves.

Based on the cost multiple, it should have been clear that Albany was headed for a decade of trouble when it came to unemployment insurance financing. In December 2000, the state had \$1.2 billion in its unemployment trust fund. While this sum may seem large, it represented only four months of unemployment trust fund reserves during a recession. By this measure, the state ranked 51st out of 53 unemployment insurance jurisdictions.⁴ The trust fund was in no position to cope with the significant recession exacerbated by the 9-11 attacks. Following the 2001 recession, the trust fund began borrowing from the U.S. Treasury in February 2002. In 2004, trust fund loans reached a peak of \$1.3 billion, a debt that would not be paid back until May 2006 when the fund finally became solvent again.⁵

There were nine states whose unemployment trust funds became insolvent in the wake of the post 9-11 recession. Of these, five states enacted solvency legislation and two used creative financing within the private market to limit the impact of borrowing on their state. Only New York and California ignored the solvency issue and took no action to minimize the immediate costs of insolvency or to improve the long-term solvency of their trust funds.⁶

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By taking no action, New York wasted several years of strong economic growth from 2004 to 2007, during which trust fund reserves could have been significantly rebuilt. Not surprisingly, on the eve of the current recession in December 2007, New York had \$429 million in its UI trust fund, enough to pay just one month of recession-level benefits. New York exhausted its trust fund by January 1, 2009 when it began borrowing from the federal government. At the end of July 2010, the state's trust fund loans stood at \$3.2 billion, trailing only Michigan and California among the 32 insolvent states. Given the size of trust fund debt, and the state's underlying UI financing problems, inaction is not a viable choice for Albany.

New York Unemployment Insurance Tax Basics

Before analyzing solutions, it is important to understand basic concepts of unemployment insurance taxation in New York State.

The taxable wage base: State unemployment insurance taxes are only assessed on a small portion of each worker's paycheck. This amount is known as the *taxable wage base*, and in New York it is a fixed at \$8,500, an amount that has been unchanged since 1999. Thus, unemployment insurance premiums are the same for part-time minimum wage workers who earn \$8,500 in a year, and would qualify for \$82 per week in UI benefits, and workers earning the state's average wage (\$55,000) or more who qualify for \$405 per week in UI benefits.

Because the taxable wage base is so low, most employers meet their full annual tax obligation in the first quarter of the year as most of their employees earn \$8,500 by the first quarter.

Tax Rates: Like all states, New York's unemployment insurance taxes are experience rated. This means that employers who lay off the most workers pay the highest unemployment tax rate and those who lay off few or no employees pay the lowest tax rate. In addition, UI taxes increase or decrease on all employers depending on the condition of the trust fund. An individual employer's unemployment insurance tax rate comes from a tax schedule that is a combination of the unemployment trust fund balance and an employer's experience rating.

Table 1 displays the minimum, average and maximum tax rates on employers in New York. Because the trust fund was insolvent in 2009, these rates represent the maximum schedule provided under law.

More than one of three employers pay the lowest rate allowed by the law in New York State, which amounts to just \$128 per employee per year and, despite trust fund insolvency, the average tax rate is still below \$400 per worker per year. While maximum tax rates can reach \$842 per employee per year, just 4 percent of employers in the state are required to pay at the top rate.⁷

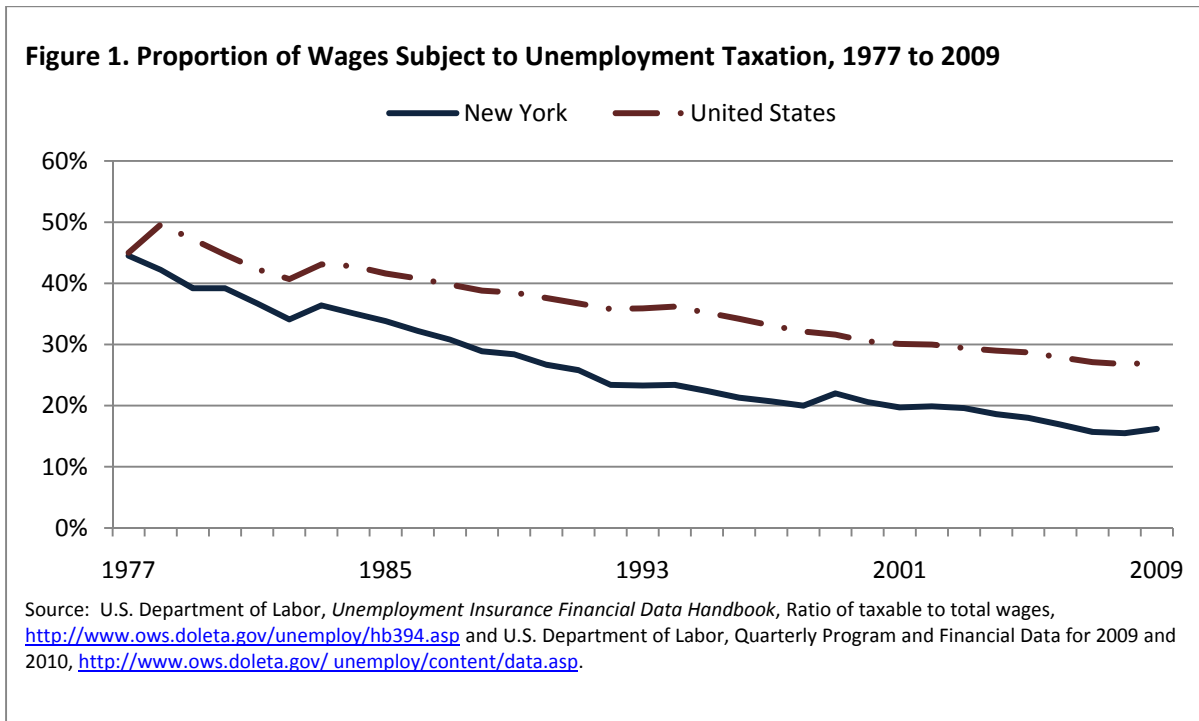
Table 1. Unemployment Insurance Tax Rates in New York, 2010

	Tax Rate (%)	Taxable Wage Base	Tax per Worker	Percent of Employers Paying at this Rate
Minimum	1.50	\$8,500	\$128	38
Average	4.68	\$8,500	\$397	N/A
Maximum	9.90	\$8,500	\$842	4

Source: New York State minimum and maximum unemployment insurance tax rates for 2010 are available at <http://www.labor.ny.gov/ui/bpta/TAXRATES.shtm>. Upon request, the U.S. Department of Labor provided NELP with average 2010 tax rates based on the ETA 205 report submitted by the state on March 31, 2010.

Taxable Wage Base is not Keeping Pace with Inflation

As a consequence of having a fixed taxable wage base, the ratio of taxable wages (those wages covered by state taxable wage bases) to total wages (those wages paid to covered employees) has declined significantly. Nationally, the ratio of taxable wages to total wages was around 45 percent in 1977 and also the same in New York State. The rate has declined across the country with just over a quarter of wages covered by UI laws subject to state UI payroll taxes in 2009. But the decline has been even more precipitous in New York State, where the taxable wage proportion fell to 26.7 percent by 1990, 20.6 percent in 2000, and all the way down to 16.2 percent by 2009 (Figure 1). In other words, New York employers are assessed UI taxes on only one out of every six dollars of wages paid in the state.



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This erosion of the taxable wage proportion is the central problem of unemployment insurance in New York State. Writing in the late 1990s, economist Philip Levine focused on fixed taxable wage bases as a key factor in UI financing.

A major deficiency in the current system of UI financing is that the infrequent, ad hoc adjustments to the taxable wage base lead to a continual erosion of its financial stability. . . . Even in the absence of severe cyclical downturns, these basic relationships indicated that the current system of UI financing will drift toward insolvency.⁸

For the most part, this description by Levine is an accurate assessment of UI financing trends over the past three decades as New York faltered towards insolvency.

The problem with fixed taxable wage bases can best be described by a comparison with another insurance program—auto insurance. New York’s low taxable wage base is analogous to an auto insurance company setting rates as if it is insuring a fleet of 1982 Ford Escorts rather than a modern-day fleet of Ford Fusions. An insurance company like that would simply go out of business, and unemployment insurance has reached a similar crisis point.

With the taxable wage base frozen at \$8,500, New York cannot recover the rising cost of benefits paid. Even though the maximum weekly benefit has been frozen at \$405 per week in New York, the average weekly benefit amount has crept up from \$231 per week to \$310 per week. With the average weekly benefit amount computed as half of a worker’s average paycheck, more and more New Yorkers are qualifying for the maximum benefit of \$405 per week.⁹ Meanwhile, the mechanisms that the trust fund has to recover these benefits are not working because the increase in unemployment taxes caused by an increase in claims paid out to a company’s former employees does not match the amount of claims that were paid out. That is because the marginal tax increase caused by an increase in claims is a percentage of the very low proportion of wages that are taxed, while benefits are based on the total amount that each worker earns.

In contrast with New York, 16 states automatically adjust their state UI taxable wage bases upward to reflect the growth of state average wages (called an “indexed” taxable wage base). This policy ensures that the basis of taxation, and thus the revenues needed to keep up with benefit payments, move in tandem with growth in the economy. Indexed taxable wage bases are frequently cited by unemployment insurance financing experts as the most important state forward financing policy.

The importance of an indexed taxable wage base can be seen in the experiences of other states (Table 2). As of June 2010, only 9 of 35 states (25 percent) that use fixed taxable wage bases were solvent. In contrast, 11 of 16 states (69 percent) with an indexed taxable wage base have managed to stay in the black more than two years after the recession hit. While an indexed taxable wage base does not guarantee solvency—**this single policy difference has made states nearly three times more likely to remain solvent than without it.** It is worth noting that all of these indexed states have much higher taxable wage bases than New York. In general, states with indexed taxable wage bases have maintained

solvency, while avoiding tax increases as well as the pressure to cut benefits when workers and employers can least afford these changes.

Table 2. States with Indexed Taxable Wage Bases

State	2010 Taxable Wage Base	State	2010 Taxable Wage Base
Alaska	\$34,100	New Mexico	\$20,800
Hawaii	\$38,800	North Carolina	\$19,700
Idaho	\$33,300	North Dakota	\$24,700
Iowa	\$24,500	Oklahoma	\$14,900
Minnesota	\$27,000	Oregon	\$32,100
Montana	\$26,000	Utah	\$28,300
Nevada	\$27,000	Washington	\$36,800
New Jersey	\$29,700	Wyoming	\$22,800

Source: U.S. Department of Labor, *Significant Provisions of State UI Laws Effective January 2010 – Revised March 2010*, <http://www.ows.doleta.gov/unemploy/statelaws.asp>.

Unemployment Insurance Tax Rates Remain Too Low

The most important comment about unemployment insurance taxes in New York is that they are low. Figure 2 shows New York State’s unemployment tax rate as a percentage of total wages paid. This effective tax rate is the best way to compare taxes over time and between states. New York’s effective tax rate has dropped from 1.1 percent in 1994 to 0.53 percent in 2008 before creeping up to 0.61 percent in 2009. This sharp decline occurred at the same time that the ***condition of the unemployment trust fund was deteriorating***—which is the exact opposite of how a self-financing system should function. Moreover, New York went from being above the national average unemployment tax rate in the mid-1990s to below the national average from 1996 to 2009—***despite the fact the unemployment trust fund ranked among the least solvent in the country*** and was clearly in need of more revenue than other states. A final reality is that neighboring states have charged more in unemployment taxes than New York in each year ***over this entire 19-year period***. Average tax rates in New York have been 30 percent lower than our neighboring states during this time.

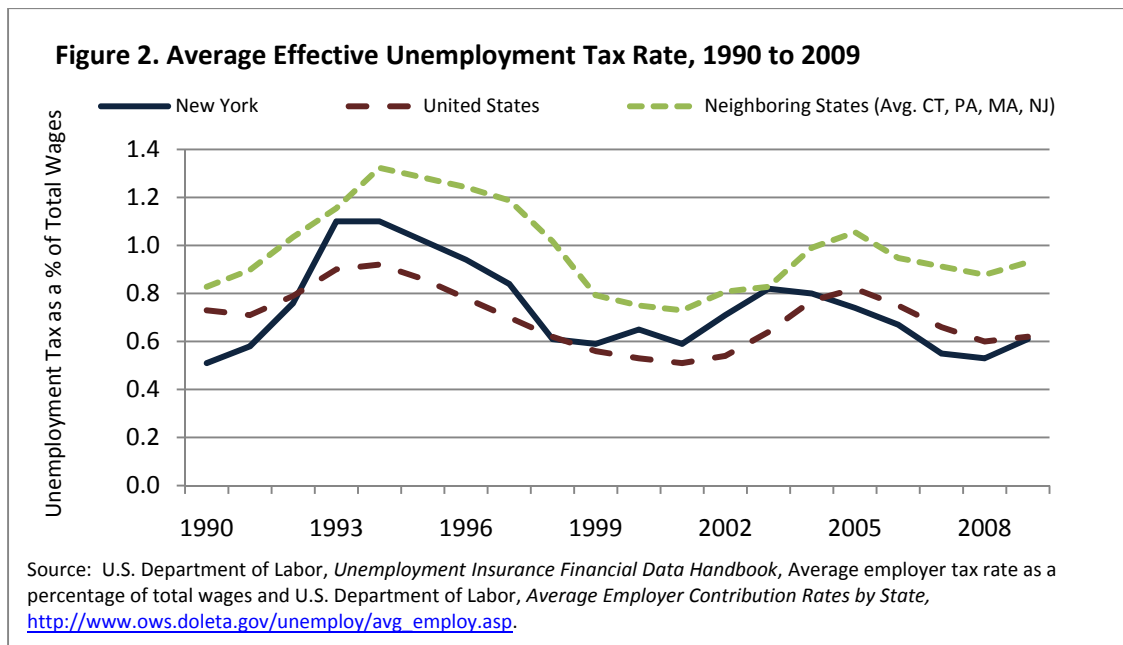
The central problem of tax responsiveness can also be illustrated through Figure 2. New York’s unemployment insurance tax rates climbed from just above 0.5 percent during the 1990-1991 recession to over 1.0 percent from 1993-1995 during the subsequent economic recovery when employers could afford to repay the significant increase in benefits. This doubling of taxes is how a counter-cyclical system should respond to a recession. The experience of the post 9-11 recession could not have been more different. Even though the trust fund was in worse shape after the 2001 recession, the revenue system did not respond in the same way. Unemployment taxes barely budged from just under 0.65 percent during the 2001 recession to 0.80 percent as the economy recovered between 2003 and 2004. The counter-cyclical mechanism simply failed.

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Why did this system fail? Most importantly, all the chargeback mechanism features in the state's tax system are assessed on only the share of wages that are taxable. With the taxable wage base so badly eroded, these incremental increases in revenue mean less and less to the effective tax rate charged to employers.

It would also be remiss not to mention generous tax reductions provided to business as part of 1998 unemployment legislation. Although the taxable wage base was increased to \$8,500 as part of that new law, this increase was not nearly enough to keep up with the growth in wages that has occurred since that time. More importantly, this legislation repealed the 0.7 percent supplemental tax on taxable wages and reduced the subsidiary taxes that are charged on all employers.¹⁰ Both of these taxes boosted the overall condition of the trust fund, and the tax reductions undermined any gains to solvency from the minimal increase in the taxable wage base. Moreover, the legislation lowered tax rates across the board for stable employers who lay off few workers.

New York was one of many states that reduced taxes in the 1990s, and these tax reductions may have seemed affordable to leaders in Albany at a time when unemployment rates were at record lows and some economists were claiming that we had solved the business cycle. Ever since the post 9-11 recession, it should have been clear that this was a short-sighted decision and that employers and the state would be better off today if they had contributed more to the trust fund during these boom years.



Albany Policy Options: Baseline Scenario not Promising

The baseline simulation prepared by the New York State Department of Labor shows a very bleak future for the unemployment trust fund. The trust fund debt is projected to surpass \$4 billion in 2011 and not return to solvency until 2018.

Table 3. Baseline Scenario for New York State's Unemployment Trust Fund

Year	Benefit Payments	NYS UI Tax Revenue Plus Interest	Interest Charges on Federal Loans	FUTA Tax Credit Reduction	Total Employer Costs	End-of-Year UI Trust Fund Reserves
2009	\$5,061	\$2,495	\$0	\$0	\$2,495	-\$2,160
2010	\$4,081	\$2,965	\$0	\$0	\$2,965	-\$3,277
2011	\$3,813	\$3,097	\$149	\$0	\$3,246	-\$3,993
2012	\$3,491	\$3,263	\$229	\$169	\$3,661	-\$4,053
2013	\$3,354	\$3,288	\$226	\$343	\$3,857	-\$3,776
2014	\$3,609	\$3,228	\$211	\$522	\$3,961	-\$3,635
2015	\$3,159	\$3,247	\$188	\$706	\$4,141	-\$2,840
2016	\$3,637	\$3,232	\$145	\$896	\$4,274	-\$2,349
2017	\$3,377	\$3,249	\$108	\$1,092	\$4,449	-\$1,385
2018	\$2,910	\$3,153	\$51	\$1,293	\$4,497	\$151
Total	\$36,492	\$31,217	\$1,308	\$5,020	\$37,545	---

Source: New York State Department of Labor, Trust Fund Simulation (Very Severe Recession), provided upon request, April 19, 2010.

Looming Employer Tax Penalties

Rather than taking action to raise employer contributions, the baseline scenario presented in Table 3 assumes that the state will pay back trust fund loans by the mechanisms of federal tax penalties. While states are not required to pay back the principal on loans in any specified time, the federal government does have automatic mechanisms to retrieve the principal. If a state has a loan balance on January 1st during two consecutive years, and cannot pay back its balance by November 1st of that year, employers in the state face a tax penalty. This penalty, known as the FUTA (Federal Unemployment Tax Act) tax credit reduction, increases the effective federal UI tax on employers in such insolvent states by \$21 per employee per year (\$21 per employee in the first year, \$42 per employee in second year, etc.) These extra revenues are used to pay back principal on the loan. New York employers faced this tax penalty in 2005 and 2006.

The baseline forecast assumes that this tax penalty (which can increase to \$378 per employee per year) will hit \$147 per employee by 2018. By this time, these extra federal taxes will be nearly 30 percent of all unemployment taxes in the state. If the economy does not fall back into recession again by 2018 this

penalty would cease in 2019. However, a serious dip in the economy could lead to an almost permanent state of insolvency with federal penalties mounting to a level approaching the state tax.

FUTA credit reductions raise many concerns for employers and state officials. The increase in the FUTA tax is confusing for employers, and requires employers to file extra paper work with their tax returns. Moreover, the FUTA credit applies equally to every employer in the state, a stark contrast to the experience-rated state tax, which varies based on each employers history of layoffs. As will be described later, the 40 percent of New York employers who pay the lowest UI tax rate would be much better off if Albany took action to pay the debt off with experience-rated state taxes.

New York Set to Waste \$1.3 Billion of Employer Tax Dollars on Interest Payments

In general, loans are interest free only between January 1st and September 30th of the same calendar year. However, because Congress (as part of the Recovery Act) waived interest on trust fund loans through 2010, interest comes due on October 1, 2011. The interest rate on loans is set to match the rate Treasury pays to states on unemployment trust fund reserves in the fourth quarter of the previous year. Had interest not been waived, this interest rate would have been 4.36 percent in 2010.

By federal law, New York cannot pay back interest from its regular state UI tax collections—which can only be used for the payment of benefits or the repayment of the principal on federal loans that were used to pay benefits. Thus, the interest payments are collected from a special interest assessment surcharge that the Commissioner of Labor appends to the unemployment tax bills sent to employers in New York State. In the baseline scenario, these interest payments will amount to a whopping \$1.3 billion by 2018, topping out at \$229 million in 2012 (Table 3).

Massive interest payments represent the short-sightedness of New York's approach to unemployment trust fund financing. Every employer dollar squandered on interest payments is not available to pay benefits, to repay the principle on trust fund loans or to accumulate reserves for the next recession. While New York had no choice but to borrow from the federal government to pay benefits to workers who had earned the right to receive them, it is nothing short of wasted money to have to pay this much in interest during a period of fiscal strain. If New York had built an adequate trust fund balance as recommended by experts, the loan amounts and interest payments would have been smaller. Moreover, New York could have earned hundreds of millions of dollars in federal interest payments on its trust fund reserves had it taken the approach of forward financing.

Current Reform Proposals Provide a Better Way Forward

Table 4 summarizes two positive proposals before the legislature in Albany to enact permanent and structural solutions to the ongoing problems of the unemployment insurance program in New York State: legislative proposal S2245B/A4921A and the Governor's proposal S8423/A11607.

Both proposals would catapult the unemployment insurance program in New York State from one of the most ill-conceived to one that would be on its way to becoming structurally sound for generations of New Yorkers to come.

Weekly Benefits not Keeping Pace with the Cost of Living

With so many New Yorkers relying on unemployment benefits, flaws in those benefits are becoming exposed. The most significant problem facing today's recipients is that benefit levels are frozen at 2000 amounts. New York's maximum benefit amount has remained unchanged for a decade at \$405 per week. At the time the maximum was set, \$405 replaced half of the average weekly wage in New York—meaning that most UI recipients who qualified for the maximum benefit would see approximately half of their paychecks replaced with UI benefits.

Since 1999, however, consumer prices increased by 27 percent nationally (and by 32 percent in the New York City metro area). While New York's average wages also increased, its maximum benefit level remained stagnant, resulting in a weekly benefit that replaces a smaller portion of the average weekly wage. Today, \$405 replaces only 36 percent of average weekly wages in the state, leaving UI recipients with less income support at a time when it is needed most.

If benefit levels kept pace with wages, New York's current maximum amount would now be \$550, 36 percent greater than the existing maximum. New York's maximum benefit amount also fares poorly when compared to that of surrounding states. In fact, New York's maximum is lower than that of all its neighboring states: laid-off workers qualify for \$600 per week in New Jersey, \$537 per week in Connecticut, \$564 per week in Pennsylvania and \$629 per week in Massachusetts. Even states that have significantly lower costs of living, such as Kansas and Arkansas, have maximum benefit amounts (\$436 and \$441, respectively) that are higher than that of New York. When each state's average weekly wage is compared to its average weekly benefit amount, New York ranks 49th out of all 50 states in terms of how well its UI benefits replace paychecks.

On the benefit side, both proposals would move New York to the best practice implemented by the 36 states that index maximum weekly benefit amounts to economic growth. By 2018, the maximum weekly benefit would be set at half of the state's average weekly wage. New York would fall near the middle of the indexed states with all but 2 of these 36 states setting their index at 50 percent or more of the state's average weekly wage, but slightly behind neighboring states, including Connecticut (60 percent), New Jersey (56.67 percent), Massachusetts (57.5 percent) and Pennsylvania (66.67 percent). On the question of maximum benefit amounts, the Governor's and Senate's proposals are more similar than different. Both end up at 50 percent of the average weekly wage, but the Governor's plan takes a more gradual approach, and also provides tougher penalties for those disqualified for benefits and who are found to have committed fraud.¹¹

On the financing side, the proposals both take the major and absolutely essential step of adopting an indexed taxable wage base. The Governor's proposal takes the conventional and most frequently

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recommended approach of incrementally increasing the taxable wage base so that it equals 18 percent of the state’s average annual wage in 2019. S2245B/A4921Bb takes the approach of giving the commissioner the discretion to raise the taxable wage base so that it covers increases in the maximum weekly benefit amount.

Taken together, these approaches ensure that the growth in revenues will track growth in benefits. The increases in the taxable wage base would not only bring more revenue into the system to pay back the loans more quickly, but it will also enable the chargeback mechanisms to function more appropriately. As employers who have laid off more employees migrate to higher tax schedules, these natural increases in employer premium levels will more effectively pay back the state because the incremental step will be charged on a higher base.

Table 4. Comparison of 2010 Unemployment Insurance Reform Proposals

Year	<u>S2245b/A4921B</u>		<u>S8423/A11607</u>		Current Law	
	Maximum Weekly Benefit ^a	Taxable Wage Base	Maximum Weekly Benefit	Taxable Wage Base	Maximum Weekly Benefit	Taxable Wage Base
2011	\$475	\$9,750	\$475	\$9,500	\$450	\$8,500
2012	\$525	\$12,500	43% of AWW	\$10,500	\$450	\$8,500
2013	\$600	\$13,500	45% of AWW	\$11,500	\$450	\$8,500
2014	\$650	Commr. Sets	45% of AWW	\$12,000	\$450	\$8,500
2015	50% of AWW	Commr. Sets	45% of AWW	\$12,500	\$450	\$8,500
2016	50% of AWW	Commr. Sets	45% of AWW	\$13,000	\$450	\$8,500
2017	50% of AWW	Commr. Sets	47% of AWW	\$13,500	\$450	\$8,500
2018	50% of AWW	Commr. Sets	50% of AWW	\$14,000	\$450	\$8,500
Index	50% of AWW	Commr. Sets	50% of AWW	18% AAW ^b	N/A	N/A

(a) AWW stands for Average Weekly Wage.

(b) AAW stands for Average Annual Wage.

Both S2245B/A4921B and S8423/A11607 would have a similar impact on state’s unemployment trust fund balance. The Department of Labor estimates that both S8423/A11607 and S2245B/A4921B would bring the trust fund back to solvency by 2015, three years ahead of the baseline scenario.¹²

It is beyond the scope of this paper to comment on which proposal is best for the legislature to enact. The bottom line is that by 2018 each proposal is identical in terms of the maximum weekly benefit amount, so from the perspective of workers the benefit levels are equal in the long run. On the financing side, an automatic increase in the taxable wage base has been consistently recommended by the U.S. Department of Labor over an approach that leaves discretion to a labor commissioner. Thus, the Governor’s approach is more optimal for UI financing.

Of course, no proposal can be enacted without the Governor’s support. Since S8423/A11607 has much to commend in it and obviously has the Governor’s support, the rest of this paper will focus on this

proposal. Thus, we will compare the fiscal impact of S8423/A11607—a proposal that will make the trust fund solvent and accumulate reserves of \$1.5 billion by 2018—with the baseline scenario. A return to solvency will also be accompanied by a long overdue increase in the maximum weekly benefit amount.

Certainly, S8423/A11607 will require employers to provided more in revenue in order to get the fund back into the black before the next recession. However, this increase is modest. The Governor’s proposal only represents a modest 11 percent tax increase over baseline employer taxes from 2009-2018. But, perhaps more importantly, S8423/A11607 would dramatically change the mix of payments required of New York employers, as displayed in Table 5.

- **Interest payments:** Wasted interest payments by employers are slashed in half from \$1.3 billion to \$614 million.
- **FUTA credit reductions:** The flat tax payment from FUTA credit reductions is cut from over \$5 billion under the baseline scenario to just \$1.7 billion. Paying back trust fund loans through experience-rated employer taxes is a fairer way to move the trust fund back to solvency than a flat tax, which unjustly burdens all employers, even those who have no layoffs.
- **Unemployment taxes for employers get reduced sooner:** Under the baseline scenario, unemployment taxes on employers continue to increase through 2018 because the federal tax penalty keeps growing throughout this period. In the Governor’s plan, by 2016, employer unemployment taxes are just over \$3.9 billion compared to the baseline scenario which leaves taxes at \$4.3 billion under the status quo.

Table 5. Impact of S8423/A11607 on New York State’s Unemployment Trust Fund

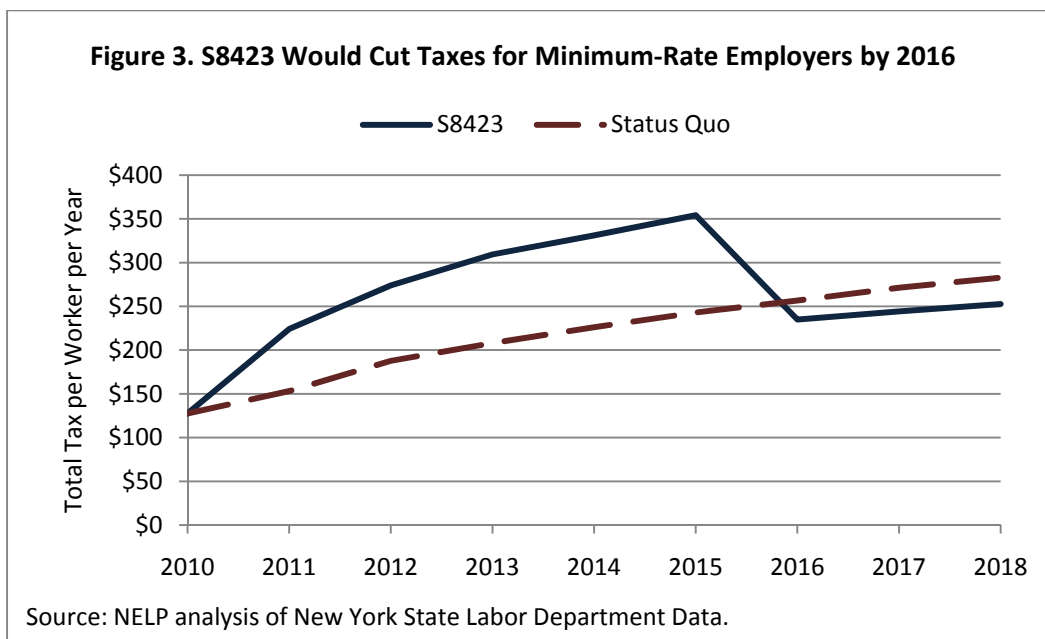
Year	UI Benefit Payments	NYS UI Tax Revenue Plus Interest	Interest Charges on Federal Loans	FUTA Tax Credit Reduction	Total Employer Taxes	End-of-Year Trust Fund Balance
2009	\$5,061	\$2,495	\$0	\$0	\$2,495	-\$2,160
2010	\$4,096	\$3,044	\$0	\$0	\$3,044	-\$3,211
2011	\$4,072	\$3,826	\$139	\$0	\$3,965	-\$3,457
2012	\$3,777	\$4,092	\$186	\$169	\$4,446	-\$2,974
2013	\$3,732	\$4,329	\$148	\$343	\$4,820	-\$2,034
2014	\$4,091	\$4,470	\$92	\$522	\$5,084	-\$1,132
2015	\$3,607	\$4,574	\$42	\$706	\$5,323	\$541
2016	\$4,184	\$3,991	\$2	\$0	\$3,993	\$348
2017	\$3,941	\$4,342	\$4	\$0	\$4,345	\$748
2018	\$3,483	\$4,274	\$0	\$0	\$4,274	\$1,540
Total	\$40,043	\$39,438	\$614	\$1,740	\$41,791	---

Source: New York State Department of Labor, Trust Fund Simulation, provided upon request, July 20, 2010

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The Governor's plan restores the counter-cyclical nature of unemployment insurance taxes. Unemployment taxes would rise gradually to \$5.3 billion by 2015 and then drop off to \$4.2 billion by 2018, thereby ensuring that taxes are at a more reasonable level if the economic recovery fizzles and benefit payments once again increase. In other words, the plan builds up reserves and pays back the trust fund during the years that are most likely to be economically healthy; so that the fund will be in better shape by the time the next recession hits.

The savings on FUTA credit reductions particularly helps stable employers achieve significant tax savings. Figure 3 shows the per employee taxes for the large group of businesses in New York State (mostly small businesses) who pay the minimum tax rate. This figure combines state taxes, FUTA credit reductions and interest payments for employers at the lowest level. Once the trust fund comes back to solvency in 2016, these employers see a significant cut in taxes under the Governor's plan as the FUTA credit reduction is no longer due. Even though the Governor's proposal requires these stable employers to put a bit more into the fund through the state tax, they will be better off in a few years because they will not be saddled with federal unemployment taxes and interest assessments.



Conclusion

Taken together, the case for unemployment reform is clear. The unemployment trust fund is in dire straits and current law will not allow for repayment until 2018. Benefits have not been increased in a decade and become less helpful to families with each passing year as the cost of living continues to increase. Fortunately, there are two viable solutions in the form of S2245B/A4921A and S8423/A11607 on the table. Both proposals would:

- Gradually increase the taxable wage base;

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- Enable employers to reduce the FUTA tax credit reduction and impending interest payments on trust fund loans;
- Return the state trust fund to solvency over a number of years; and
- Index weekly benefit amounts to keep pace with economic growth.

Reforms outlined in these proposals would go a long way toward creating a strong and viable unemployment insurance system that is there for workers when the next Great Recession strikes.

Notes

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² The estimated number of workers benefiting from unemployment insurance (1.8 million) is the sum of first payments from December 2007 through the end of June 2010. This figure does not account for jobless workers who were already receiving unemployment benefits before December 2007. There may also be some double counting due to the fact that a number of unemployed workers who moved in and out of employment since December 2007 may have received multiple “first payments.” First payments data is available through the U.S. Department of Labor’s Monthly Program and Financial data at <http://www.ows.doleta.gov/unemploy/claimssum.asp>.

³ Wayne Vroman, *Topics in Unemployment Insurance Financing*, p. 10.

⁴ This includes the 50 states, the District of Columbia, Puerto Rico and the Virgin Islands.

⁵ U.S. Treasury Department, Bureau of the Public Debt, Unemployment Insurance Trust Fund Report Selection, New York Transaction Statements for 2002 to 2010, http://www.treasurydirect.gov/govt/reports/tfmp/tfmp_utf.htm.

⁶ Wayne Vroman, “The Recession of 2001 and Unemployment Insurance Financing,” January 2005, Urban Institute.

⁷ ETA 204 form Data provided by the New York State Department of Labor upon request.

⁸ Phillip B. Levine, “Financing Benefit Payments,” in Christopher J. O’Leary and Stephen A. Wandner, ed., *Unemployment Insurance in the United States: Analysis of Policy Issues*, (Kalamazoo, Michigan. Upjohn Institute, 1997), p. 332.

⁹ Technically benefits are equal to 1/26th of a worker’s total high-quarter wages, but for workers who have steady earnings this is equivalent to half of the average wage.

¹⁰ Fiscal Policy Institute, “An Agenda for New York: Modernizing Unemployment Insurance in New York State.”

¹¹ The more pertinent concern with the Governor’s proposal is that it includes increases in various types of penalties. One penalty makes it harder for claimants to re-qualify for UI benefits after they quit or fired from a job, a change that will bring down the number of workers eligible for UI benefits. A second change imposes a 25 percent penalty on workers who are found to have a factually false statement or to have willfully misrepresented their situation in order collect UI benefits. The primary purpose of this extra penalty is to provide a stronger financial disincentive for individuals who blatantly bilk the system by working and collecting UI benefits. Those who directly represent UI claimants have expressed a concern that some claimants who make a mistake during the application process or apply for UI after confusing circumstances are also charged with a willful misrepresentation, and that these charges are often reversed upon appeal—and are concerned that the added penalty will negatively impact those who are not able to obtain legal representation. If these stronger penalties are put into place, it will be important for the Labor Department to continue efforts it has already begun to make sure that these damaging findings of willful misrepresentation are only put into place when there is true fraud occurring.

¹² New York State Department of Labor, “Results Summary UI Benefits, Revenues, Reserves,” provided to author upon request, July 2009.