NELP

National Employment Law Project

UNEMPLOYMENT INSURANCE FINANCING:
STATE TRUST FUNDS IN RECESSION AS OF SEPTEMBER 30, 2008

Introduction

In May 2008, NELP issued a briefing paper (*Unemployment Insurance Financing: Examining State Trust Funds Facing Recession*). Using U.S. Department of Labor data for the end of calendar year 2007, we described the solvency status of state unemployment insurance (UI) trust funds. We found that taken as a whole, state UI trust funds were less prepared for recession at the end of 2007 when compared to their status prior to the 2001 recession. We also found that some 18 states had particularly low UI trust fund reserves, while a fairly large group of 21 states had reserves sufficient for a moderate recession.

In light of the nearly unprecedented financial market upheaval that has taken place in the U.S. over the last month, we are revisiting UI financing by issuing this solvency update. The chances of a short or mild recession now look less likely than they did in May, while the potential for a moderate or severe recession is more likely. This update uses UI financial data from the end of the third calendar quarter 2008 to bring the story of state UI trust fund solvency up to September 30, 2008.

State UI Trust Fund Solvency Overview as of September 30, 2008

Unemployment numbers have risen in every month of 2008, and UI claims numbers have risen steadily as well. At the end of December 2007, the seasonally adjusted 4-week moving average for new state UI claims was 343,750 a week. This figure had risen to 474,250 weekly new claims by the end of September 2008, representing an increase of 38 percent in new claims over this nine-month period. Insured unemployment rose from 2.694 million (seasonally adjusted 4-week moving average) to 3.563 million by the end of September. This translates to an increase of 869,250 weekly insured unemployed workers, or a rise of 32 percent in insured unemployment.

Increased unemployment hurts UI solvency in two ways. First, UI claims and benefit payments rise. Second, since jobless workers are not earning wages, state UI payroll tax collections fall as unemployed workers' wages exceed taxable wage base levels and are no longer subject to payroll taxation. These two factors have taken a toll on UI solvency during the first three quarters of 2008. States' trust fund reserves had fallen to $36.7 billion by September 30, 2008, a 10 percent decline from a year ago when they stood at $40.8 billion.[1] Since December 31st of last year, trust fund balances have dropped more than 1.5 billion in the last nine months alone.

For this update, Table 1 compares average monthly UI payments in each state over the past 12 months to that state's trust fund balance as of September 30. This calculation produces a number representing months of current average UI benefit payments that each state's trust fund reserves can sustain without relying upon any incoming UI payroll tax revenues. (We use this methodology in this update as a shorthand method of rating state solvency pending U.S. Department of Labor releasing its more standard solvency measures sometime early next year.) Our method here roughly approximates that used to calculate the average high cost multiple, a commonly used solvency measure.

Our updated solvency analysis of more recent state level UI financial data confirms our earlier views. As of September 30, 2008, we see in Table 1 that:

- Not Solvent: Five states (Michigan, Indiana, New York, South Carolina, and Ohio) have reserves covering 3 months or less of their average monthly UI payments.
- Nearly Insolvent: Eight states have reserves covering 4 to 6 months of average payments (New Jersey, California, Kentucky, Missouri, Wisconsin, North Carolina, Rhode Island, and Arkansas).
- Marginally Solvent: Another six states have balances that fall into the 7 to 11 month range when compared to current benefit payment levels (Pennsylvania, Minnesota, Idaho, Illinois, Connecticut, and Massachusetts).

In short, 19 states make up a group of nearly insolvent or marginally solvent states. In comparison, 20 states have 24 months of average benefit payments or more in their current reserves (from least to most: Colorado, New Hampshire, Iowa, Kansas, Arizona, Hawaii, Oregon, Alaska, Nebraska, Montana, North Dakota, New Mexico, Maine, DC, Mississippi, Washington, Oklahoma, Utah, Wyoming, Louisiana). The remaining states fall into a middle range of solvency.

In our earlier paper, we found at the end of 2007 that four states had UI trust funds that were basically not solvent (MI, MO, NY, and OH) and another 14 states fell well below recommended solvency levels (AR, CA, IL, IN, KY, MN, NC, NJ, PA, SC, SD, TN, TX, and WI). Another eight states (AL, CO, CT, ID, MA, RI, VA, WV) were deemed likely to face financing difficulties in a moderate to severe recession. At the same time, we found 21 states with healthy UI trust fund levels, grouping 13 states (AK, HI, ME, MS, MT, NM, OK, OR, PR, UT, VT, WA, WY) as very solvent with another eight states near recommended solvency levels (AZ, DC, FL, LA, NE, NV, NH, VI). In short, most states fell roughly into two groups, those with UI trust fund reserves above or near recommended levels of solvency and those without adequate reserves.

Solvency Outlook for 2009

September 30 is a particularly apt time to judge trust fund solvency. On average, states only impose UI payroll taxes on the first $11,500 of each worker's wages (termed "taxable wage base"). With average yearly wages over $43,000 (earnings in covered employment), most employers pay their UI payroll tax obligations in the first 2 quarters of the year in most states. This is because UI taxes are paid only on wages falling below each state's taxable wage base level. Consequently, UI payroll tax revenues fall significantly in most states in the last two calendar quarters of each year. As a result, most states are unlikely to collect significant revenue between now and April 2009, when first quarter 2009 tax payments are due. For this reason, states that have less than three months of reserves at this point are in serious risk of insolvency. States with four to six months of reserve are also in danger of insolvency depending on their particular cash flows in the coming months, especially if layoffs rise more steeply with a declining economy.

Recent reports confirm that states anticipate difficulties meeting their benefit obligations. Already Michigan has taken out a federal trust fund loan with an outstanding balance of $376 million as of October 2nd. California predicts an unemployment trust fund deficit of $2.7 billion in 2009.[2] South Carolina's Employment Security Commissioner has told the Greenville News that the state expects to borrow from the federal government in the first quarter of 2009[3]. Published reports state that Ohio projects deficit near the end of 2009.[4] A spokesperson for the Indiana Department of Workforce Development acknowledges the possibility of borrowing in the first quarter of 2009.[5]

It is particularly troubling that so many states are facing insolvency so early in this economic downturn. For most states, 2008 represents the first time in several years that UI benefit payments have exceeded payroll tax revenues—and this reversal is already depleting reserves to zero or near zero levels. With all of the negative economic trends, it is likely that benefit payments will exceed trust fund revenues for several years, and these shortfalls threaten to leave a number of states deep in debt by 2010. While short term loans to states from the federal government are interest-free, such long term deficits bear federal interest costs or potential federal tax penalties to employers in those states.

Adequate unemployment insurance benefits are particularly vital to the economy now. Thus, states should be especially vigilant to make sure benefit levels are high enough to enable families to make ends meet and that workers are not left out of the safety net. Still, the solvency outlook should focus the attention of state legislative leaders in troubled states as they look towards 2009 legislative sessions. States with solvency issues have the opportunity to prevent large and lasting trust fund deficits by enacting policy changes that begin to bring their systems into balance. The impact of solvency legislation in 2009 would likely take effect at the start of the 2010 tax year—by which point the economy will hopefully begin expanding again. Action is particularly needed in those states (like California and South Carolina) where solvency problems have worsened even as taxes in 2008 are already at the highest levels provided for by current state law.

Should Federal UI Trust Funds Bail Out Insolvent States?

Those states that currently have solvency problems have, with one or two exceptions, had UI trust fund reserves below recommended levels for years. Given the number of years that it takes states to work themselves out of solvency difficulties, and the necessity of raising taxes to do so, most states have chosen to simply not concern themselves with UI financing, hoping that they can muddle through.

In a misguided effort to assist states, a distribution of federal UI trust funds (known as a Reed Act distribution) was made in March 2002. With very limited exceptions, instead of using these $8 billion in federal funds as a jump start on restoring state trust fund solvency or to expanding benefits, states used the federal dollars exclusively as a means to reduce state UI payroll tax rates. Long term state solvency was not significantly boosted. Recently, some states and governors have advocated another Reed distribution of federal trust funds. We opposed such a distribution.

Rather than simply bailing out less solvent states by giving them federal UI trust funds dollars, NELP and other allies have advocated using federal trust fund distributions to reward states that have adopted beneficial state UI rules or that take these measures in the future. This approach was embodied in the UI Modernization Act, which passed the House of Representatives in October 2007 as part of a larger bill (H.R. 3920). A closely similar bill remains before the Senate (S. 1871). UI Modernization is a better approach than a Reed Act bailout. It rewards states that have more adequate UI safety nets while creating incentives for those without acceptable UI programs to bring them up to higher standards. And, bolstering UI programs is an effective way to stimulate our economy and help affected communities, workers, and employers.

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Endnotes

[1] U.S. Department of Treasury, Bureau of Public Debt, Unemployment Trust Fund Report, September 30, 2008 and UI quarterly data summary, September 30th, 2007.

[2] "California May Run Out of Money for Unemployment," San Bernandino Sun, October 8, 2008.

[3] "State jobless fund is low," Greenville News, September 9, 2008.

[4] "Ohio's unemployment insurance trust fund nears empty," Business First of Columbus, June 20, 2008.

[5] "Indiana Government Withstanding Financial Meltdown," Associated Press, September 9, 2008.

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State Unemployment Insurance Trust Fund Savings
As of September 30, 2008

	September 30th Trust Fund Balance (millions)	Current Monthly Benefit Payout (millions)	Number of Months Saved
Michigan	-$340.3	$164.9	0
Indiana	$90.7	$66.1	1
New York	$475.8	$204.6	2
South Carolina	$102.5	$34.6	3
Ohio	$334.0	$114.0	3
New Jersey	$792.9	$177.0	4
California	$1,785.2	$495.7	4
Kentucky	$194.4	$39.5	5
Missouri	$221.6	$40.6	5
Wisconsin	$413.6	$78.2	5
North Carolina	$439.8	$88.2	5
Rhode Island	$114.0	$21.1	5
Arkansas	$151.3	$25.7	6
Pennsylvania	$1,483.8	$208.7	7
Minnesota	$574.1	$67.5	9
Idaho	$128.1	$14.8	9
Connecticut	$566.7	$54.0	10
Illinois	$1,849.3	$170.6	11
Massachusetts	$1,403.9	$130.3	11
Tennessee	$558.6	$39.2	14
Florida	$1,767.8	$125.4	14
Texas	$1,671.4	$111.1	15
Virgin Islands	$15.2	$1.0	15
Delaware	$153.8	$9.4	16
South Dakota	$28.2	$1.6	18
Alabama	$395.5	$21.7	18
Georgia	$1,151.4	$63.1	18
Vermont	$154.0	$8.4	18
Maryland	$896.7	$44.4	20
Nevada	$714.6	$35.8	20
Virginia	$731.0	$35.3	21
West Virginia	$250.0	$11.8	21
Colorado	$699.9	$29.1	24
New Hampshire	$196.3	$8.3	24
Iowa	$756.6	$30.1	25
Kansas	$635.6	$22.8	28
Puerto Rico	$539.0	$17.2	31
Arizona	$964.5	$29.2	33
Hawaii	$485.5	$13.9	35
Oregon	$2,121.6	$55.3	38
Alaska	$346.8	$9.0	39
Nebraska	$296.9	$7.7	39
Montana	$282.0	$7.1	40
North Dakota	$137.6	$3.3	42
New Mexico	$543.8	$12.3	44
Maine	$466.7	$10.4	45
District of Columbia	$423.0	$9.0	47
Mississippi	$717.4	$12.3	58
Washington	$4,117.7	$70.8	58
Oklahoma	$856.2	$13.7	62
Utah	$851.3	$12.4	69
Wyoming	$258.7	$3.4	76
Louisiana	$1,483.9	$15.8	94

Source: Labor Department, Treasury Department