

Unemployment Insurance Solvency Act of 2011 (S.386)

- **Current UI Financing Crisis:** Coming out of the worst recession since World War II, 30 states have insolvent unemployment trust funds and have borrowed over \$46 billion in outstanding federal loans; debt could climb to \$65 billion. Many states will not be able to pay back their federal loans by the end of this decade and may hit another recession prior to restoring solvency.
- The Unemployment Insurance Solvency Act was introduced on February 17, 2011 by Senators Durbin (D-IL), Reed (D-RI) and Brown (D-OH)

Legislative Goals

- Provide immediate relief to borrowing states from federal interest costs, and to employers from automatic federal unemployment tax increases necessary to make principal payments.
- Help restore the state systems to solvency over time while rewarding solvent states that have in place responsible UI financing policies.
- Help protect benefits from cuts while states voluntarily agree to restore solvency and receive partial loan forgiveness.
- Remain deficit-neutral, with state revenues raised over the life of the legislation for state unemployment funds held in the federal treasury.

Primary Provisions

- (1) **Extends the waiver of interest on federal loans to states for two years (for 2011 and 2012).** From 2009 through 2010, federal law provided states with a waiver of interest on their federal loans to pay state UI benefits. This bill extends the interest waiver for 2011 and 2012.

Impact: Waiving interest payments for two additional years saves about 30 states \$3-4 billion in federal interest payments.

- (2) **Postpones employer tax hikes to repay the principal on states' federal loans until 2014.** Currently, after the second year of borrowing, employers in states with outstanding federal loans are required to begin paying higher federal (FUTA) taxes to repay principal. For most borrowing states, employers would see their FUTA taxes on

2011 wages increase from \$56 to \$77 per worker (payable in January 2012), and then to \$98 per worker for 2012 wages (payable in 2013). This bill gives employers relief from these FUTA tax increases for taxable years 2011 and 2012. Instead, FUTA tax increases (called "FUTA credit reductions") that would be assessed under current law on 2012 and 2013 wages would first come not come due until January 2014.

Impact: Delaying FUTA credit reductions for two years saves employers an estimated \$5 billion.

- (3) **Increases the federal "taxable wage base" from \$7,000 to \$15,000 starting in 2014, but reduces the FUTA tax rate to maintain the same total federal taxes paid per worker.** In addition, the federal taxable wage base would increase each year. The bill continues the current 6.2 percent FUTA rate through 2013, but reduces the rate to 5.78 percent in calendar year 2014 when the wage base increase takes effect. This keeps the actual FUTA tax paid by employers at the current yearly amount of about \$56 per employee.

Impact: Of the 31 borrowing states, 23 have state taxable wage bases below \$15,000 and therefore need to enact increases by 2014. There are currently 15 borrowing states with taxable wage bases below \$10,000 and 13 of these states account for nearly three-quarters of all borrowing to date. Indexing the federal wage base to wage growth will likely mean the federal minimum will increase over \$15,000 in 2015. Nineteen states currently have taxable wage bases at \$15,000 or higher and 16 of those states are already indexed to wage growth.

- (4) **Allows states to enter into voluntary agreements to incrementally reduce up to 60 percent of the federal loan balances in return for assurances of state actions leading to trust fund solvency.** The high level of existing debt is creating much pressure in some states to cut unemployment benefits even while unemployment is still very high. Given the amount of state borrowing, it will be difficult for states to pay back their loans, let alone prepare for the next recession. Thus, additional relief is needed to provide states with incentives to not only pay back their loans, but to adopt responsible financing reforms that will prepare their systems for another recession.

Under this bill, borrowing states can apply for abatements on the principal of the state loans up to 60 percent, subject to voluntary agreements with the U.S. Department of Labor that the state will eventually reach adequate levels of reserves sufficient to pay benefits in the event of another severe recession. Agreements can last up to seven years. Most states will qualify for 60 percent principal abatement (determined based on the balance of the loan in effect as of December 2011, or when the bill is enacted,

whichever is later). Upon approval of the state's solvency plan by the U.S. Department of Labor, the transfer of the annual amount of the principal abatement is made to the state's trust fund on December 31st and thereafter on a yearly basis assuming compliance with the plan.

States that elect to enter voluntary agreements with the U.S. Department of Labor to substantially reduce the amount of principal to be repaid on their federal loans also make assurances that they will not reduce unemployment benefits or impose new restrictions on eligibility for benefits during the life of the agreement.

Impact: Because each state's decision to enter into an abatement agreement is voluntary, it is difficult to assess the overall costs. If all borrowing states entered into agreements, loan forgiveness would likely range from \$24-37 billion. This would be offset by gradual increased revenues resulting from increases in state taxable wage bases.

- (5) **Creates new rewards and incentives for the states that maintain solvent unemployment trust funds.** Recognizing that a number of states were well prepared to pay benefits in the event of severe recession, and that other states and their employers should be incentivized to do so in the future, the bill includes additional provisions that reward states that reach the recommended levels of solvency.

For those states that maintain one year of reserves sufficient to pay benefits during a severe recession (1.0 Average High Cost Multiple), the bill provides:

- Additional interest (0.5 percent over the current market rate of interest) on the state trust funds held by the U.S. Treasury. The additional interest may be used by states to support the administration of their UI programs and for other purposes authorized by the Reed Act.
- The FUTA tax on employers would be reduced by \$14 per worker in states with solvent trust funds

Impact: Based only on increased taxable wage bases and the loan forgiveness provisions required by the bill, 8 states would meet the federal solvency goal (1.0 AHCM) now or by 2015, and 29 states would reach the goal by 2020. These states would receive the benefit of a projected \$5.4 billion in FUTA tax cuts and increased trust fund revenues through incentives offered under the bill.