3B

UI Taxes and Business Climate

Question: Have state UI payroll taxes risen over the decades?

Answer: No. Employer UI contribution rates reached an all-time low prior to the start of the Great Recession in 2008. The recession was preceded by a period of neglect for UI financing. Between 1995 and 2005, 31 states reduced UI taxes by at least 20 percent. As a result of these tax cuts, and an overall failure to keep state taxable wage bases aligned with growth in wages, state UI payroll taxes as a percentage of wages fell to an all-time low during the first decade of the 2000s (Table 1). Compared to the 1990s, the percentage of unemployed workers who actually receive regular benefits remained below 40 percent, and the generosity of benefits relative to wages (i.e., the wage replacement rate) was unchanged for decades. As we've noted elsewhere, in 2014 the recipiency rate for regular UI programs reached its lowest levels in UI program history (27 percent).

Table 1. How an average claimant earning $300 fares in states with different partial UI rules

Decade	Recipiency Rate (% of unemployed receiving UI)	Replacement Rate (average weekly benefit as a % of average weekly wages)	Employer Contribution Rate (% of total wages)
1950s	49%	33%	0.98%
1960s	42%	35%	1.10%
1970s	38%	36%	1.00%
1980s	35%	36%	1.11%
1990s	36%	35%	0.76%
2000s	39%	35%	0.65%

Source: Employer contribution and replacement rates are from the U.S. Department of Labor, Financial Data Handbook 394. Recipiency rate is for regular state UI from the U.S. Department of Labor, Unemployment Insurance Chartbook.

UI payroll taxes have increased in most states since the Great Recession. These increases were a result of the increased claims arising from the economic downturn and the failure of some states to accumulate trust fund reserves during the years prior to the Great Recession. In CY 2014, average state UI taxes on total wages were 0.81 percent, well within the range of UI taxes in prior decades. Taxes or surcharges were notably higher in recent years in those states that are repaying federal UI loans or using municipal bonds to replenish their UI trust funds.

Question: How do the costs of unemployment insurance stack up with other employer costs for wages and benefits?

Answer: Unemployment insurance costs are modest relative to wages and employee benefits. For each dollar of wages earned by workers, businesses pay less than one cent in federal and state UI taxes. On average, private sector workers earn $33 of wages and benefits for each hour worked (Table 2). Of this total amount, UI accounts for only 23 cents an hour. Compared with other benefits, such as health care and paid leave, UI makes up a small fraction of total compensation. The portion of compensation attributable to UI increased since the start of the recession as a result of automatic tax increases resulting from insolvent state trust funds. But because UI costs are minor relative to wages and other benefits, the UI-related increase accounted for only four cents of a total compensation increase of $2.17 between 2007 and 2011. And, cost increases for UI payroll taxes leveled off after 2011, and remained only 23 cents in 2014.

Table 2. Private Employer Costs Per Hour for Wages and Benefits

	2007	2011	2014
Total compensation	$26.09	$28.26	$33.49
Wages and salaries	$18.44	$19.93	$22.88
Total Benefits			$10.61
Insurance (i.e., health, life, and disability)	$1.99	$2.28	$2.97
Paid leave	$1.78	$1.92	$2.33
Social Security and Medicare	$1.55	$1.66	$1.84
Retirement and savings	$0.91	$1.02	$1.78
Federal and state unemployment insurance	$0.19	$0.23	$0.23

Source: U.S. Department of Labor, Bureau of Labor Statistics, National Compensation Survey, Table 1- Employment Cost Trends, for March 2008, 2012 and 2015, accessed August 4, 2015. Note that not all benefit subgroups are listed.

Question: How have corporate profits fared since the economic downturn?

Answer: Corporate profits remain near all-time highs as a percentage of GDP and in comparison to personal (individual) income. As a result of rising corporate profits and lagging employment, the share of national income going to corporations increased substantially during the post-recession recovery period, and remained close to record levels in 2014. In comparison, employee compensation including wages and benefits, as a percentage of national income, has fallen steadily from a historical peak in 1980 to a 45-year low.

As discussed above in our UI financing section, most UI experts recommend that states build UI trust fund reserves during years when the economy is growing and corporate profits are higher. Failure to finance trust funds in advance of recessions means that UI payroll taxes will be raised during or soon after a recession. This approach reduces the counter-cyclical role expected from UI programs.

Question: Are unemployment insurance payroll taxes important to a state's business climate?

Answer: The entire discussion of business climate is fraught with overheated arguments and unsupported claims. Nonetheless, business groups and their allies certainly believe (or act like they believe) there is some reality underlying their arguments that creating a "good business climate" impacts business location and economic development in each state. And, UI programs are frequently caught up in this argument with many public officials, pundits, and other participants in these discussions viewing UI as a key component of state business climate. Since state officials accept this concept, UI advocates need some familiarity with it.

To begin, readers can get good background about business climate debates in Greg LeRoy's book, The Great American Job Scam: Corporate Tax Dodging and the Myth of Job Creation as well as in Peter Fisher's "Grading Places: What Do the Business Climate Rankings Really Tell Us?" These and other works cast doubt on the whole idea that business site selection or job creation can be pegged to something falling under the category of business climate.

Generally, employer groups focus on average UI payroll tax rates and maximum tax rates when making their business climate arguments about UI taxes. In most states, large majorities of employers pay the minimum state UI tax, so getting information about the distribution of state payroll taxes is one key step in countering these arguments. Regardless of the dollar amount of a state's average tax rate, that average rate matters much less if 70 percent of a state's employers pay a lower minimum UI tax rate. Similarly, in most states a minority of employers pay the maximum UI rate. State UI tax distribution information can be obtained from the U.S. Department of Labor's Significant Measures of State UI Systems.

In addition, UI taxes should be discussed in terms of total wages, rather than the much lower level of taxable wages (as noted in our UI financing discussion, state taxes are imposed only on a smaller amount called the "taxable wage base"). Finally, some attention to the direction or trend of state UI taxes is important. Although UI taxes naturally increased as a result of the Great Recession, in the majority of states, UI tax levels are trending toward or have returned to pre-recession levels.

Comparisons between a state's UI taxes to other factors included in the business climate argument will show that UI is not as significant a factor as many others. Nearly all these comparison items will be much larger than UI taxes, whether you compare UI taxes with other state taxes, typical costs of production, utilities, or other employment-related costs. As shown above, state UI taxes average less than 25 cents of total hourly employment costs (or 0.69 percent). It should be harder for critics of UI to make a credible business climate case against UI once they are forced to discuss specifics, rather than just making abstract claims.

Resources:

Mike Evangelist, "Lessons Left Unlearned: Unemployment Insurance Financing After the Great Recession," Policy Brief, National Employment Law Project (July 2012).

Peter Fisher, Grading Places: What Do the Business Climate Rankings Really Tell Us? Washington, DC: Economic Policy Institute (2005).

Greg LeRoy, The Great American Job Scam: Corporate Tax Dodging and the Myth of Job Creation. San Francisco, Barret-Koehler (2005).

U.S. Department of Labor, Significant Measures of State UI Tax Systems 2014, (posted August 2015), http://workforcesecurity.doleta.gov/unemploy/pdf/sigmeasuitaxsys14.pdf.

Wayne Vroman, Topics in Unemployment Insurance Financing. Kalamazoo, MI: Upjohn Institute for Employment Research (1998).

Wayne Vroman, Unemployment Insurance Trust Fund Adequacy in the 1990s. Kalamazoo, MI: Upjohn Institute for Employment Research (1990).

Wayne Vroman, "Financing Unemployment Insurance after the Great Recession," Brief, Urban Institute (August 2012).