

**GAO**

Report to the Chairman, Subcommittee  
on Income Security and Family Support,  
Committee on Ways and Means, House of  
Representatives

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April 2010

# UNEMPLOYMENT INSURANCE TRUST FUNDS

## Long-standing State Financing Policies Have Increased Risk of Insolvency



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**Highlights**

Highlights of [GAO-10-440](#), a report to the Chairman, Subcommittee on Income Security and Family Support, Committee on Ways and Means, House of Representatives

**Why GAO Did This Study**

The federal-state unemployment insurance (UI) program relies on state trust funds to hold enough reserves to meet benefit needs during economic downturns. The sufficiency of such “forward funding” has been a policy concern for decades, particularly during the recent recession, which has caused very high unemployment rates. While the economy added jobs in March 2010, unemployment remains very high and has continued to rise in most states, suggesting that state UI programs will continue to face serious financial challenges for at least the near future.

This report (1) describes the current condition of state UI trust funds, (2) highlights policies or practices that have contributed to their conditions, and (3) identifies options for improving UI forward funding in the future. To address these questions, GAO analyzed statistics from the Department of Labor, reviewed applicable laws and regulations, interviewed state UI representatives and UI experts, and synthesized GAO’s and others’ findings to present policy options.

**What GAO Recommends**

The Congress should begin to consider options to improve trust fund solvency, including raising the FUTA taxable wage base from its current level of \$7,000 and indexing this base to average annual wages. GAO received comments from the Department of Labor that generally concur with our findings and conclusions.

[View GAO-10-440 or key components.](#)  
For more information, contact Andrew Sherrill at (202) 512-7215 or [sherrilla@gao.gov](mailto:sherrilla@gao.gov).

**UNEMPLOYMENT INSURANCE TRUST FUNDS**

**Long-standing State Financing Policies Have Increased Risk of Insolvency**

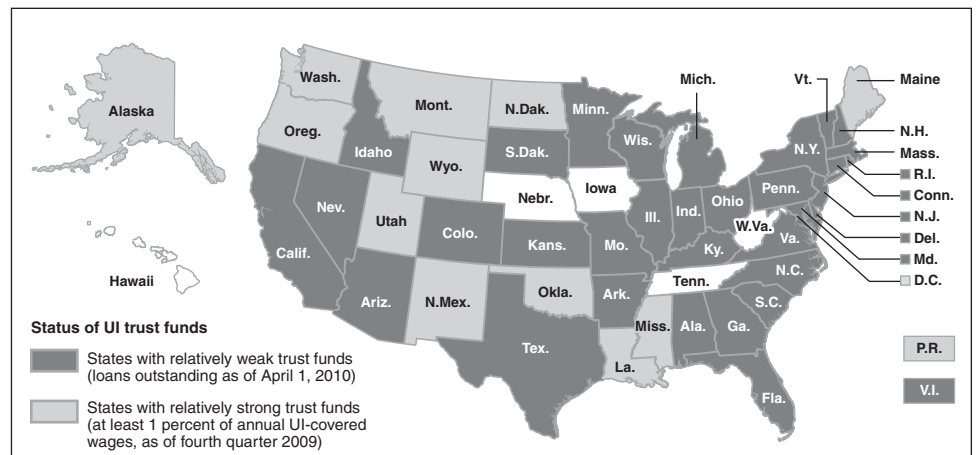
**What GAO Found**

By any measure, state UI trust funds are in historically poor financial condition. As of April 1, 2010, 34 of the 53 state trust funds have outstanding loans totaling \$38.9 billion from the federal government to pay benefits (see figure), and as of the end of 2009 no state had enough reserves to cover 12 months of benefits at historically high rates. Aggregate reserves net of loans measured -\$15.4 billion as of the end of 2009, the lowest level in the program’s history. Despite UI tax rates that are expected to rise significantly in many states in 2010, the Department of Labor projects that net UI reserves will remain negative for several years.

Long-standing UI tax policies and practices in many states over 3 decades have eroded trust fund reserves, leaving states in a weak position prior to the recent recession. While benefits over this period have remained largely flat relative to wages, employer tax rates have declined. Specifically, most state taxable wage bases have not kept up with increases in wages, and many employers pay very low tax rates on these wage bases.

Options to improve state UI trust fund financial conditions include raising and indexing the taxable wage base under the Federal Unemployment Tax Act (FUTA), which could induce many states to raise and index their own bases, and reducing the number of both employers paying very low rates and those that pay less in UI taxes than benefits paid to their former workers. Other options include adjusting state tax rates more frequently; raising solvency targets before lowering rates; setting additional conditions to receive interest-free federal loans; and raising interest credits for well funded trust funds. Now is the time to consider changes to policies to improve the long-term financial structure of UI trust funds.

**Financial Condition of State UI Trust Funds**



Source: Employment and Training Administration, Department of Labor.

Note: States highlighted in white did not have an outstanding loan as of April 1, 2010, and had trust funds with less than 1 percent of wages in reserves as of fourth quarter 2009.

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## **Abbreviations**

AHCM	average high cost multiple
ARRA	American Recovery and Reinvestment Act of 2009
CBO	Congressional Budget Office
CRS	Congressional Research Service
DOL	Department of Labor
EB	Federal-State Extended Benefits Program
ES	Employment Services
ESAA	Employment Security Administration Account
ETA	Employment and Training Administration
EUC	Emergency Unemployment Compensation Program of 2008
EUCA	Extended Unemployment Compensation Account
FECA	The Federal Employees Compensation Account
FUA	Federal Unemployment Account
FUTA	Federal Unemployment Tax Act
HCM	high cost multiple
IUR	insured unemployment rate
UI	unemployment insurance
UTF	Unemployment Insurance Trust Fund

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United States Government Accountability Office  
Washington, DC 20548

April 14, 2010

The Honorable Jim McDermott  
Chairman  
Subcommittee on Income Security and Family Support  
Committee on Ways and Means  
House of Representatives

Dear Mr. Chairman:

The recession that began in December 2007 has resulted in the worst labor market conditions in the United States since at least the early 1980s, if not since the Great Depression of the 1930s. The federal-state unemployment insurance (UI) program provides temporary assistance to unemployed workers by replacing a portion of lost wages. States maintain reserves, funded through employer taxes, in trust funds, out of which they pay UI benefits. However, the severity and length of the recent recession, and the slow pace of recovery, have placed a heavy demand on state UI trust funds, and many states have needed loans from the federal government to continue to pay benefits. While preliminary data showed that the economy added the most jobs in any month in 3 years during March 2010, unemployment remains very high and has continued to increase in most states, suggesting that state UI programs will continue to face serious financial challenges for at least the near future.

Concerns over the adequacy of UI trust fund levels are not new. For the last 3 decades and particularly during prior recessions, there has been concern that some states were not sufficiently funding their programs. Two national commissions, one in the early 1980s and the other in the mid-1990s, have examined UI financing, as did GAO in 1988, 1990, and 1993. Each of these studies raised concerns that long-term state practices in UI financing have been insufficient to fulfill the goals of the UI program—to ease individual financial hardship and stabilize the economy in periods of unemployment.

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This report (1) describes the current condition of state UI trust funds; (2) highlights policies or practices that have contributed to their condition; and (3) identifies options for improving UI forward funding in the future.<sup>1</sup>

To address these issues, we reviewed UI state statistical data for fiscal years 1979 to 2009 from the Department of Labor's (DOL) Employment and Training Administration (ETA). With these data, we analyzed various measures of individual UI state trust fund levels that illustrate the condition of state trust funds. We also reviewed applicable federal and state laws, regulations and guidance. We reviewed reports by GAO, DOL, the Congressional Budget Office (CBO), the Congressional Research Service (CRS), public policy organizations, and conducted interviews with DOL officials and UI policy experts from the business, labor, academic, and public policy communities. To illustrate key factors affecting UI funding in states, we conducted in-depth interviews with UI program officials from 10 states that represent a range of geographic locations, economic conditions, and UI trust fund reserve levels. We supplemented these interviews with information from related state and federal reports. Finally, to identify options for improving UI forward funding, we reviewed past conclusions and recommendations in reports by GAO, DOL, CBO, CRS, four past government advisory councils on unemployment compensation, and public policy organizations, and supplemented this analysis with our own conclusions derived from our analysis of UI state statistical data.

We conducted this performance audit from May 2009 through April 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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<sup>1</sup>The term "forward funding" usually refers to budget authority that is made available for obligation beginning in the last quarter of the fiscal year for the financing of ongoing activities (usually grant programs) during the next fiscal year. GAO, *A Glossary of Terms Used in the Federal Budget Process*, [GAO-05-734SP](#) (September 2005). However, in this report we use "forward funding" to refer to the practice of states accumulating reserves in unemployment insurance trust funds in anticipation of increased outlays in the future.

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## Background

The Social Security Act of 1935 established the UI program.<sup>2</sup> The primary objectives of UI are to provide temporary, partial compensation for lost earnings of individuals who become unemployed through no fault of their own, with some exceptions, and to stabilize the economy during economic downturns.<sup>3</sup> The UI program is a federal-state partnership. Although federal law sets certain requirements for the program, each state designs its own program within the framework of the federal requirements. State and federal taxes on employers fund UI benefits and administrative costs. The ETA's Office of Unemployment Insurance oversees the states' implementation and administration of their UI programs.<sup>4</sup>

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## UI Federal and State Requirements

Federal law sets forth broad coverage provisions for the categories of workers that must be covered by the program, some benefit provisions, the federal tax base and rate, and administrative requirements, such as how states will repay UI trust fund loans. Within the framework established by federal law, states can determine key elements of their UI programs, such as eligibility/disqualification provisions, the benefit amount, and the amount of taxes that employers must pay.

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## UI Eligibility

States use varying methods to determine eligibility for a claimant to receive UI benefits, but all states set a base period of wages and employment on which to determine a worker's benefit rights, the benefit year during which UI may be collected, and the maximum amount of regular UI that a worker may receive in a benefit year. States generally base benefits on wages for work in covered employment over a 12-month

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<sup>2</sup>Pub. L. No. 74-271.

<sup>3</sup>Some states allow for some workers who quit for certain work-related or personal reasons to be eligible for UI benefits. The American Recovery and Reinvestment Act of 2009 (ARRA) Pub. L. No. 111-5, Div. B, § 2003 authorized the Secretary of Labor to make unemployment compensation modernization incentive payments to states that amend their laws to allow UI payments to individuals who quit employment for certain compelling family reason such as following their spouse to a new job.

<sup>4</sup>We use the term "states" to refer to the administrative entities of the 53 unemployment insurance programs that cover the 50 states, the District of Columbia, Puerto Rico, and the Virgin Islands.



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period, and most states currently pay regular benefits for up to 26 weeks.<sup>5</sup> Extended benefits (EB) are provided to workers who have exhausted regular unemployment insurance benefits during periods of high unemployment.<sup>6</sup> The EB program is financed in approximately shares by the states and the federal government. The basic EB program provides up to 13 additional weeks of benefits. Some states have also enacted a voluntary program to pay up to 7 additional weeks (20 weeks maximum) of EB during periods of extremely high unemployment. This program is in addition to and differs from other temporary emergency UI measures passed by the Congress in recent recessions, such as the Emergency Unemployment Compensation (EUC) program enacted in 2008<sup>7</sup> and provisions in the American Recovery and Reinvestment Act (ARRA) of 2009.<sup>8</sup>

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## UI Financing

The UI program was designed to be forward funded and self-financed by states, with each trust fund building up reserves from employer taxes during periods of economic expansion in order to pay UI benefits during economic downturns. Because unemployment can vary substantially during a business cycle, it is important that states build sufficient trust funds to remain solvent during recessionary times. The program is financed primarily by taxes levied on employers.<sup>9</sup> Each state sets UI tax rates to finance regular UI benefits. In addition, employers pay a Federal Unemployment Tax Act (FUTA) tax. The FUTA tax on employers is 6.2 percent on the first \$7,000 of each employee's annual pay.<sup>10</sup> Employers in states whose UI programs comply with federal requirements receive a tax

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<sup>5</sup>Almost all wage and salary workers are covered by the UI program. Federal civilian employees and ex-service members are covered under separate programs administered by the states for the federal government and paid for by the various federal agencies or military departments. Railroad workers are covered under a program administered by the Railroad Retirement Board.

<sup>6</sup>Federal-State Extended Unemployment Compensation Act of 1970, Pub. L. No. 91-373, Title II 26 U.S.C. § 3304, note.

<sup>7</sup>Supplemental Appropriations Act, 2008, Pub. L. No. 110-252. As provided in Pub. L. No. 111-144, the EUC08 program has been extended through April 5, 2010.

<sup>8</sup>Under ARRA, as amended by Pub. L. No. 111-144, the federal government is financing 100 percent of EB benefits through April 5, 2010. For more discussion of UI-related measures in ARRA, see appendix II.

<sup>9</sup>Alaska, New Jersey, and Pennsylvania also withhold UI taxes from employee wages.

<sup>10</sup>26 U.S.C. § 3301.

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rate credit of 5.4 percent, resulting in an effective rate as low as 0.8 percent, or a maximum of \$56 per worker per year.<sup>11</sup> The FUTA tax is used to fund: (1) federal and state UI administration costs;<sup>12</sup> (2) the federal share of EB; (3) Title XII loans to state trust funds when they cannot pay benefits;<sup>13</sup> (4) benefits under federal supplemental and emergency programs; (5) labor exchange services,<sup>14</sup> employment and training for veterans; and (6) some labor market information programs.

States choose both a taxable wage base, the annual earnings per worker on which employers pay UI taxes, and statutory tax rates that apply to the base. In order for employers in their state to qualify for the full FUTA tax credit, each state's taxable wage base must at least equal the FUTA wage base (currently \$7,000, the level since 1983), and statutory rates must be experience rated—that is, varying with an employer's layoff record. Experience ratings provide reduced rates for employers with fewer layoffs and increased rates for those with more layoffs. Tax rate assignment may include “socialized” costs that are not charged to individual employers, such as costs of benefits to employees of firms that went out of business but did not have sufficient reserves to pay UI taxes or benefits that are charged to a specific employer but are not fully recovered from that firm in tax revenue.<sup>15</sup>

The Unemployment Insurance Trust Fund (UTF) in the U.S. Treasury consists of 53 state accounts, including one each for the District of

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<sup>11</sup>26 U.S.C. § 3302.

<sup>12</sup>GAO has conducted past reports on UI administrative funding and problems states have had with funding technologies to improve the efficiency and integrity in administering the program. See GAO, *Human Service Programs: Demonstration Projects Could Identify Ways to Simplify Policies and Facilitate Technology Enhancements to Reduce Administrative Costs*, GAO-06-942 (Washington, D.C.: Sept. 19, 2006); and *Unemployment Insurance: Increased Focus on Program Integrity Could Reduce Billions in Overpayments*, GAO-02-697 (Washington, D.C.: July 12, 2002).

<sup>13</sup>Title XII of the Social Security Act, 42 U.S.C. §§ 1321 - 1324.

<sup>14</sup>Labor exchange services include job search assistance, job referral, placement assistance for job seekers, re-employment services to UI claimants, and recruitment services to employers with job openings.

<sup>15</sup>See GAO, *Unemployment Insurance: States' Tax Financing Systems Allow Costs to Be Shared Among Industries*, GAO-06-769 (Washington, D.C.: July 2006), for a more detailed discussion of experience rating. Some states levy social cost taxes to recover uncollected benefit costs, such as those paid to unemployed individuals but not charged to the firms for whom the employers had worked. See table 10 in appendix IV for more details.

Columbia, the Virgin Islands, and Puerto Rico, plus 6 federal accounts that are dedicated for special purposes. Federal taxes go into the Employment Security Administration Account (ESAA), the Extended Unemployment Compensation Account (EUCA), and the Federal Unemployment Account (FUA), and state taxes go into their individual state accounts (see table 1).

**Table 1: Summary of Major UI Federal Accounts**

<b>Name</b>	<b>Description</b>
ESAA	Finances the administration of the state UI and employment services (ES) programs.
EUCA	Reimburses states for federal share of extended benefits. Permanent extended benefits program provides up to 13 weeks of additional UI benefits
FUA	Provides loans to insolvent state trust funds.
The Federal Employees Compensation Account (FECA)	Finances benefit payments to former federal and military employees

Source: ETA, Comparison of State Unemployment Insurance Laws, January 1, 2009.

Note: In addition, there are two accounts related to the Railroad Retirement Board that pay UI benefits to railroad workers, the only occupational group covered under a separate UI system. They are financed by railroad contributions and administered by the Railroad Retirement Board.

When the ESAA, EUCA, and FUA accounts reach prescribed statutory ceilings, the excess funds are transferred to individual state accounts under the Reed Act.<sup>16</sup> DOL bases each state's share of Reed Act funds on the state's proportional share of FUTA taxable wages. Federal law restricts states to use Reed Act distributions, the mechanism by which the federal government gives surplus cash back to states, only to cover the cost of state benefits and administration of state UI and ES programs. A state must have a specific appropriation from its legislature in order to use its share of the Reed Act funds for administrative expenses.<sup>17</sup> There have been eight Reed Act distributions since 1956, most recently in 2002; the

<sup>16</sup>The term Reed Act refers to a part of the Employment Security Financing Act of 1954, Pub. L. No. 83-567. The provisions referred to are found in Title IX of the Social Security Act, 42 U.S.C. §§ 1101-1110.

<sup>17</sup>42 U.S.C. § 1103(c)(2).

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Congress has raised the Reed Act's statutory ceilings that trigger the distribution of the surplus funds several times.<sup>18</sup>

Almost all states measure their trust fund balances and make tax rate changes once per year.<sup>19</sup> The majority of states have trust fund balance targets written into their state law, with triggers built in to adjust the tax rates according to the state's trust fund balance. According to DOL, most states impose higher tax rates when their UI balances are low and lower rates when their balances are high. Nearly half of states with targets base them on a percentage of their payrolls or specific dollar amounts. For example, New York requires the equivalent of at least 5 percent of its annual payrolls in its trust fund to enact its lowest tax schedule; the highest schedule applies when the trust fund is less than zero percent of the payroll. Other states have trust fund targets that are based on other measurements of trust fund levels, such as state-determined experience or adjustment factors and some states do not have specific UI trust fund goals in their laws. For example, 4 of the 53 states have laws that authorize their labor agencies to set the tax rates. State trust funds are credited with interest on their balances.

As UI is forward-funded, states collect trust fund reserves in advance to pay benefits. However, during exceptional periods when states exhaust their UI reserves, they may borrow from the federal government. States can, under certain conditions, borrow interest free, as long as the loan is repaid by September 30 of the year of the loan (a "cash flow" loan).<sup>20</sup> If a state has an outstanding loan balance on January 1 for 2 consecutive years, the full amount of the loan must be repaid by November 10 of the second year, or employers in that state lose 0.3 percent of the FUTA tax

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<sup>18</sup>For more information on congressional changes to the Reed Act's statutory ceilings, see Congressional Research Service, *The Unemployment Fund and Reed Act Distributions*, RS22006 (Washington, D.C.: Feb. 17, 2009).

<sup>19</sup>New Hampshire allows for quarterly adjustments to tax rates based on quarterly measurements of the trust fund, and Tennessee can activate 6-month tax schedules.

<sup>20</sup>42 U.S.C. § 1322(b)(2). In addition to repaying a loan by September 30 the state may not have another advance during the calendar year and must meet funding goals established under regulations issued by the Secretary of Labor. The requirement that Labor establish funding goals was added by the Balanced Budget Act of 1997 (Pub. L. No. 105-33, § 5404). Labor has published proposed rules on funding goals which have yet to be finalized. See 74 Fed. Reg. 30,402 (June 25, 2009). ARRA provided that all loans from the federal government are interest-free until December 31, 2010, 42 U.S.C. § 1322(b)(10) (as added by Pub. L. No. 111-5, Div. B, § 2004).

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credit each year there is an unpaid balance. For example, if a state borrows to pay UI benefits and has an outstanding loan balance on the second subsequent January 1, the FUTA tax credit falls from 5.4 to 5.1 percent, and employers' effective FUTA rate jumps from 0.8 percent to 1.1 percent. However, states with outstanding loans can still seek relief from these loan provisions. If state trust funds meet specific requirements, such as not taking any action during the previous year that would diminish the solvency of their trust fund, the reduction in the FUTA credit may be capped.<sup>21</sup> States that have an average total unemployment rate of 13.5 percent or more<sup>22</sup> can also delay payment of interest for a grace period of up to 9 months.<sup>23</sup> Some states have also chosen to secure loans in the private bond market, using the proceeds from private loans to repay borrowing from the federal government, and then levying higher payroll taxes on employers in subsequent years to repay the private loans.

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## Measures of UI Solvency

Measures of UI solvency are expressed as a percentage of wages, typically total annual wages earned by employees who are potentially eligible for receiving UI benefits (or "UI-covered wages").<sup>24</sup> ETA reports reserve ratios, or UI trust fund levels as a percentage of total annual statewide wages, as well as high cost multiple (HCM), which divides the reserve ratio by the high cost rate, the highest historical ratio of benefits to wages for a 12-month period in that state. An HCM of 1.0 corresponds to sufficient reserves to pay benefits at the high cost rate for 1 year. A similar measure is the average high cost multiple (AHCM), which divides a trust fund's reserve ratio by the average high cost rate, which is the average of the 3 highest calendar year benefit cost rates in the last 20 years or in the period covering the last 3 recessions, if longer. An AHCM of 1.0 is the target level of solvency recommended by the Advisory Council on Unemployment Compensation and is inherent in DOL's draft regulations on cash-flow loans.

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<sup>21</sup>See 26 U.S.C. § 3302(f).

<sup>22</sup>This rate of 13.5 percent or greater is for the most recent 12-month period for which data are available.

<sup>23</sup>42 U.S.C. § 1322(b)(9).

<sup>24</sup>Unless stated otherwise, in this report "total wages" are total wages in UI-covered employment.

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## Past Studies of UI Trust Fund Solvency

UI reform, particularly with respect to financing the program, has been a longstanding (albeit sporadic) policy concern for the federal government, state workforce agencies that administer the program, and advocacy organizations. A 1980 national commission expressed concerns about the “financial footing” of the program,<sup>25</sup> while a 1988 GAO report raised questions about the effect of long-term UI financing inadequacy on future benefit eligibility.<sup>26</sup> A 1988 study of the program by the CRS highlighted the problem of insufficient financing.<sup>27</sup> In addition, a 1993 GAO report found that the ability of the UI program to stabilize the economy had diminished,<sup>28</sup> and a 1994-96 Advisory Council on Unemployment Compensation called for a stronger role for the federal government to promote UI forward funding.<sup>29</sup>

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## State UI Trust Funds Are at Historically Weak Levels, with Most Requiring Federal Loans to Pay Benefits

By any measure, UI trust funds nationwide are in historically poor financial condition. As of the fourth quarter of 2009, reserves in state trust funds totaled \$11.1 billion, lower than any end-of-year total (inflation adjusted) in the program’s history and down sharply from the \$30.0 billion in aggregate reserves at the end of 2008. Reserve levels look even weaker when one considers that fund levels are buoyed by federal loans, which surged during 2009 and continue to grow. As of April 1, 2010, 34 state trust funds had taken out federal loans totaling \$38.9 billion (see fig. 1); this total loan balance is up almost 50 percent since just December 31, 2009. By comparison, 24 states required loans during the recession of the early 1980s, during which unemployment nationally approached 11 percent. Aggregate net reserves (reserves less loans) as of December 31, 2009, measured -\$15.4 billion, the first such deficit since the end of 1983 and the lowest level in the program’s history. As a result of the huge outflow of money to state trust funds, the FUA has had to borrow \$33.9 billion from

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<sup>25</sup>National Commission on Unemployment Compensation, *Unemployment Compensation: Final Report* (July 1980).

<sup>26</sup>GAO, *Unemployment Insurance: Trust Fund Reserves Inadequate*, [GAO/HRD-88-55](#) (Washington, D.C.: Sept. 26, 1988).

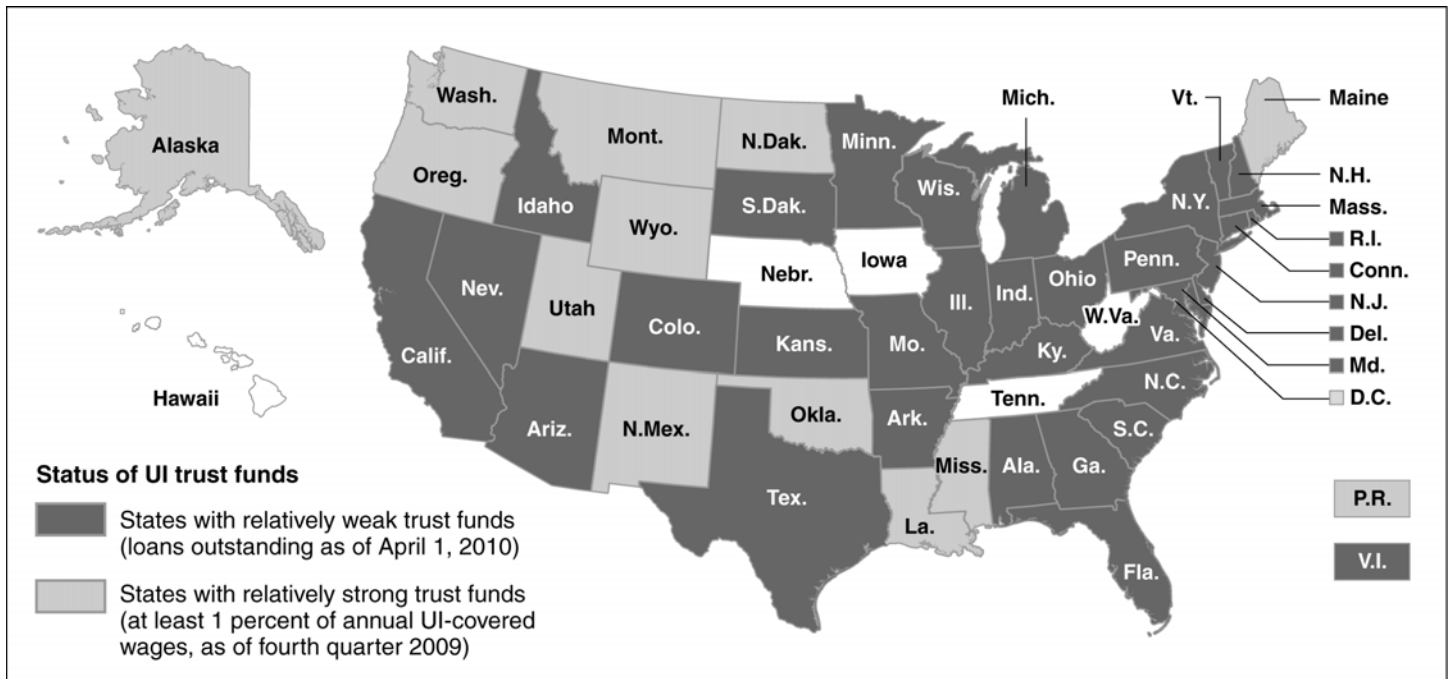
<sup>27</sup>*Federal State Unemployment Compensation System: A Study Prepared by the Congressional Research Service of the Library of Congress* (Washington, D.C.: Sept. 8, 1988).

<sup>28</sup>GAO, *Unemployment Insurance: Program’s Ability to Meet Objectives Jeopardized*, [GAO/HRD-93-107](#) (Washington, D.C.: Sept. 28, 1993).

<sup>29</sup>Advisory Council on Unemployment Compensation, *Defining Federal and State Roles in Unemployment Insurance* (Washington, D.C.:1996).

the general fund as of April 7, 2010; the Department of Labor projects FUA borrowing to more than double by 2012.

**Figure 1: Financial Condition of State UI Trust Funds**



Source: Employment and Training Administration, Department of Labor.

Note: States highlighted in white did not have an outstanding loan as of April 1, 2010, and had trust funds with less than 1 percent of wages in reserves as of fourth quarter 2009. For more data, see appendix IV, table 7.

As of the fourth quarter of 2009, no state had a HCM as high as 1.0 (which would indicate sufficient reserves to pay benefits at historically high rates for 12 months), and only 14 states had reserves of at least 1 percent of wages (see fig. 1). Each state trust fund had a lower balance as of the end of 2009 than as of the end of 2007, near the start of the recent recession in December 2007 (see table 2). In aggregate, state trust fund balances declined by \$53.6 billion over this period.

**Table 2: State UI Trust Fund Financial Conditions as of End of 2007 vs. End of 2009**

	12/31/2007		12/31/2009	
	Net trust fund balance (thousands of dollars)	High-cost multiple	Net trust fund balance (thousands of dollars)	High-cost multiple
AK	\$331,214	0.78	\$298,439	0.64
AL	410,640	0.33	-137,148	N.A.
AR	151,132	0.18	-208,639	N.A.
AZ	990,481	0.44	168,909	0.08
CA	2,533,133	0.18	-5,873,815	N.A.
CO	630,397	0.59	64,579	0.06
CT	598,111	0.23	-140,878	N.A.
DC	400,275	0.80	329,696	0.66
DE	174,156	0.43	38,828	0.10
FL	2,203,889	0.46	-816,194	N.A.
GA	1,281,787	0.42	-51,955	N.A.
HI	556,334	1.50	130,687	0.35
IA	740,178	0.69	383,905	0.36
ID	196,048	0.35	-103,659	N.A.
IL	1,801,983	0.30	-1,159,558	N.A.
IN	306,787	0.20	-1,469,630	N.A.
KS	637,983	0.71	119,794	0.14
KY	230,766	0.16	-566,263	N.A.
LA	1,444,768	0.82	1,144,195	0.63
MA	1,290,297	0.28	234,162	0.05
MD	1,016,659	0.52	135,304	0.07
ME	479,164	1.12	335,162	0.82
MI	-103,489	N.A.	-3,044,026	N.A.
MN	545,587	0.30	-271,487	N.A.
MO	113,246	0.07	-460,468	N.A.
MS	727,918	1.32	469,903	0.89
MT	280,512	0.82	166,822	0.50
NC	394,426	0.13	-1,587,455	N.A.
ND	134,442	0.72	98,997	0.47
NE	278,865	0.74	167,832	0.44
NH	240,422	0.43	17,905	0.04
NJ	650,449	0.11	-894,641	N.A.
NM	575,524	1.58	281,026	0.79
NV	793,215	0.63	-85,593	N.A.



	12/31/2007		12/31/2009	
	Net trust fund balance (thousands of dollars)	High-cost multiple	Net trust fund balance (thousands of dollars)	High-cost multiple
NY	429,723	0.04	-2,118,436	N.A.
OH	444,530	0.09	-1,692,542	N.A.
OK	831,388	1.42	488,513	0.80
OR	1,933,225	1.14	1,050,277	0.65
PA	1,545,652	0.25	-1,754,681	N.A.
PR	529,260	0.73	397,376	0.56
RI	159,901	0.25	-125,592	N.A.
SC	199,183	0.13	-682,073	N.A.
SD	24,680	0.25	-6,510	N.A.
TN	566,161	0.30	167,600	0.10
TX	1,774,694	0.40	-1,282,382	N.A.
UT	842,680	1.15	492,923	0.71
VA	775,202	0.44	-53,882	N.A.
VI	22,287	0.68	-7,577	N.A.
VT	177,613	0.72	23,038	0.10
WA	3,794,156	0.98	2,596,130	0.67
WI	592,228	0.23	-895,714	N.A.
WV	244,786	0.35	123,859	0.17
WY	243,500	0.95	155,048	0.60
<b>Total</b>	<b>\$38,168,149</b>	<b>0.36</b>	<b>-\$15,409,890</b>	<b>N.A.</b>

Source: Employment and Training Administration, U.S. Department of Labor.

Note: Net trust fund balances are gross reserves less federal UI loans. 'N.A.' for high-cost multiple indicates a negative net trust fund balance.

## Recent Recession Has Sharply Increased Number and Duration of UI Claims

The recent recession has resulted in very large numbers of workers receiving benefits for very long periods of time. The insured unemployment rate (IUR), which provides a measure of the percentage of the UI-covered labor force receiving benefits, reached 4.6 percent in the second quarter of 2009, higher than any annual level since reaching 4.7 percent for 1982.<sup>30</sup> Twenty-three states recorded quarterly rates of 4.7 percent or higher during the second quarter of 2009. Unemployed workers

<sup>30</sup>The IUR is the average weekly number of insured workers divided by the sum of average monthly UI-covered employment and average monthly "reimbursable" employment, which includes the UI-covered public and nonprofit sectors. A state's IUR is typically much lower than its total unemployment rate because many unemployed workers do not qualify for benefits, typically because of low applications, eligibility denials, or benefit exhaustion.

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have also experienced an historically long duration of benefit reciprocity during this recession. Nationally, the average duration among those workers receiving benefits during the fourth quarter of 2009 was 18.8 weeks, higher than any annual average in the program's history.<sup>31</sup> For 2009, total weeks compensated for regular UI claimants totaled 266 million, also higher than that of any year in the program's history.

High IURs and long durations have increased demands on the UI program. Total UI regular and extended benefits paid out in 2009 equaled \$85.8 billion, compared to \$40.7 billion for all of 2008. The highest 12-month benefit payout rate, 2.2 percent of total wages, occurred in 1975, but 2009 could approach that level of benefit payments.<sup>32</sup> Another indicator of the surge in benefit payments is that 40 states paid extended benefits in the fourth quarter of 2009; these benefits totaled \$6.3 billion in 2009, higher in inflation-adjusted terms than in any year since 1976.

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### Although UI Tax Rates Will Rise Sharply in Many States, Labor Projects Negative Balances for Several Years

UI taxes in most states will increase in 2010, and likely beyond, because of automatic triggers in most states that react to declining UI trust fund reserves. Twenty-five states have raised their UI taxable wage base in 2010, including 9 that do not index the base to average wages. A 2009 state survey found that 35 states would increase their UI taxes on employers in 2010, with increases ranging from 2.5 percent in Kentucky to 600 percent in Hawaii, and a median projected contribution level increase of 27.5 percent.<sup>33</sup> The survey also found that 10 other states indicated that they could not increase their tax schedules any further under current state law, and would need to have their state legislatures revise current law to do so.

Despite projected tax increases in many states, UI reserves are expected to decline sharply in the near future. While the economy appears to be recovering from the recession, DOL has projected that national unemployment rates will remain well above 9 percent in 2010, and

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<sup>31</sup>Duration figures reported by ETA equal the number of weeks compensated during the year divided by the number of first payments. The figures may include more than one period of continuous unemployment. It excludes all unemployment for which no benefits were paid, such as waiting periods, disqualifications, and any time after exhaustion of benefits.

<sup>32</sup>Because total wage data are incomplete for 2009, we cannot yet calculate this percentage.

<sup>33</sup>National Association of State Workforce Agencies (NASWA), *UI Trust Fund Solvency Survey* (December 2009). Florida, Hawaii, Indiana, and Massachusetts all took action in their 2010 legislative sessions to limit the impact of scheduled rate increases.

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according to the CBO, many professional forecasters predict that the pace of the recovery will be slow and that unemployment will remain high for several years. DOL estimates that state UI regular benefit outlays will be at \$74.9 billion in fiscal year 2009 and \$93.3 billion in fiscal year 2010, which is almost triple the amount of UI benefits paid out in fiscal year 2007. DOL has projected that trust fund account balances, net of loans, will fall to -\$88.4 billion at the end of fiscal year 2012 before starting to grow again, with net balances not becoming positive until well beyond fiscal year 2014. DOL anticipates that the number of outstanding UI loans that states have from the federal government will increase until 2012, when they could total \$90 billion. Employers in states that cannot make their loan payments within the required 2-year period could lose some of their FUTA tax credit and pay increasing tax rates each year until the loan is repaid. For example, a 2009 UI solvency study by the state of New Hampshire projected that if the state's employers lose FUTA tax credits in 2012, they will owe an additional \$153 million in taxes through 2016, plus an additional \$71 million in 2017. During past recessions in the 1980s and 2000s, employers in approximately 20 states did lose FUTA tax credits due to states' inability to repay state loans on time, and the federal government ultimately kept the escalating FUTA credit reductions in place until the states repaid their debts.<sup>34</sup>

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## Long-standing State UI Policies and Practices Have Led to Trust Fund Vulnerability

While the recent recession has severely drained UI reserves, the current situation reflects long-term financial decline. The mid-1970s marked a noticeable shift in trust fund financial conditions, starting with the recession that lasted from 1973 to 1975. Prior to that time, from 1938 to 1973, state UI trust funds held average year-end reserves, net of loans, equal to 5.1 percent of wages, and never dropped below 2 percent. From 1974 to 2008, that average fell to 1.0 percent of wages and has never been as high as 2 percent. Therefore, states have had less of a financial buffer in their trust funds to withstand a high-cost benefit period. Prior to the recent recession, the aggregate HCM nationwide was only 0.35, corresponding to enough reserves for about 4 months of benefits at a high-cost rate; therefore even a much milder recession was likely to have caused widespread trust fund insolvency. Further, table 3 shows a large difference in the average state HCM prior to the current recession for states that have needed to borrow to pay benefits (average state HCM of 0.32) and those that have not (0.87), with similar pre-recession funding differences for the

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<sup>34</sup>A state can avoid its employers' FUTA tax credit reduction for a year by making repayments of a certain amount prior to November 9 of that year. 26 U.S.C. § 3302(g).

three previous recessions.<sup>35</sup> This suggests that pre-recession funding levels have played a key role in helping states avoid loans during the recent recession and current recovery (although the average peak IUR in borrowing states has also exceeded that of non-borrowing states). Further, average U.S. pre-recession funding levels were lower prior to the recent recession than for the previous three. Perhaps most surprising is that despite a 10-year economic expansion prior to the 2001 recession, states built up trust funds to an average HCM of only 0.64, enough to pay benefits at a high-cost rate for about 8 months.

**Table 3: Key Trust Fund and Employment Statistics for Last Four U.S. Recessions**

Date of recession	2007		Early 1980s		1990		2001	
	Pre-recession HCM	Peak IUR	Pre-recession HCM	Peak IUR	Pre-recession HCM	Peak IUR	Pre-recession HCM	Peak IUR
States taking out federal loans (number of states)	0.34 (34)	4.9	0.28 (25)	5.2	0.34 (5)	3.7	0.30 (5)	2.7
Non-borrowing states	0.93	4.2	0.96	4.6	1.01	3.1	0.91	2.7
All U.S.	0.35	4.6	0.41	4.7	0.86	3.2	0.64	2.8

Source: GAO calculations, based on Unemployment Insurance Financial Data Handbook, ETA.

Note: HCM is average state high cost multiple just prior to recession and IUR is average peak state insured unemployment rate following onset of recession (annual data for 1980s and 1990, quarterly for 2001 and 2007). All U.S. is not an average of state measures.

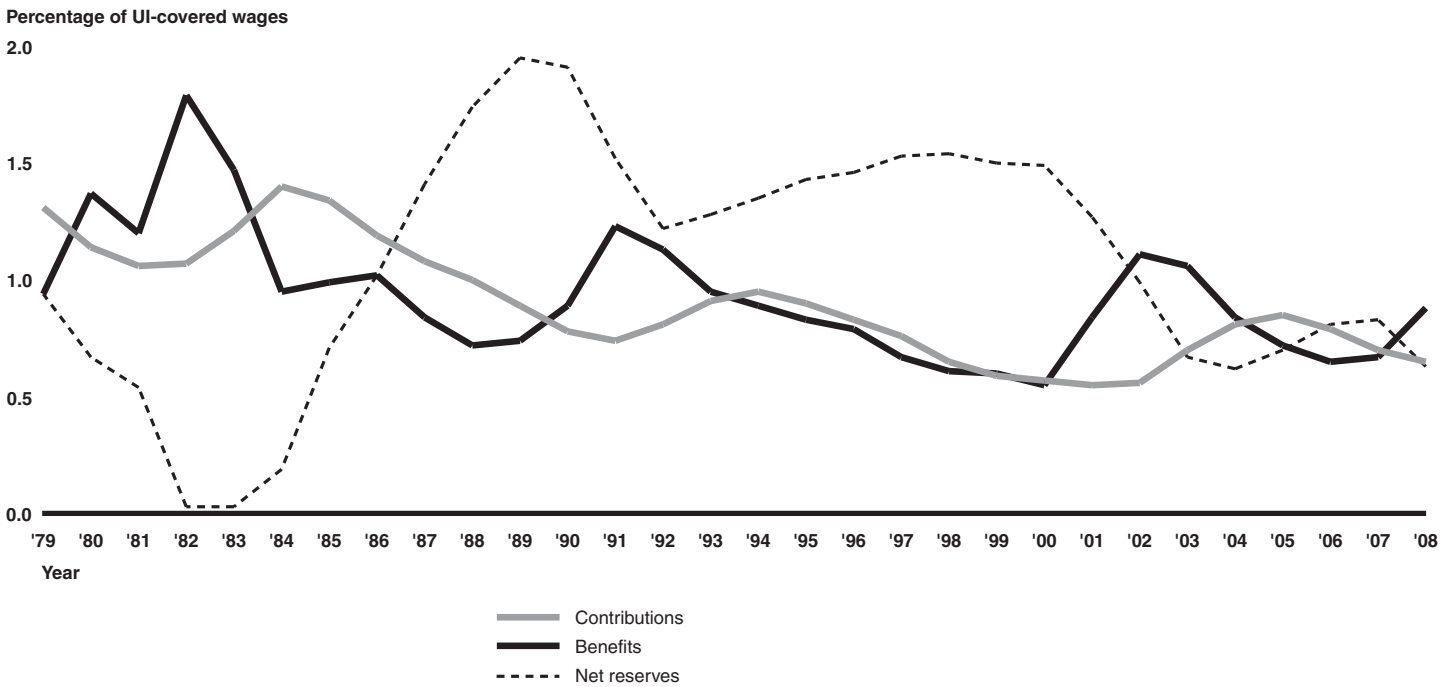
<sup>35</sup> Although the government does not officially set dates for the start and end of recessions, business cycle dates announced by the National Bureau of Economic Research (NBER) Business Cycle Dating Committee are widely accepted. While the committee does not set hard criteria for defining recession, most of the periods defined this way consist of two or more quarters of declining gross domestic product. For more on NBER's process for determining business cycle dates, see [http://www.nber.org/cycles/recessions\\_faq.html](http://www.nber.org/cycles/recessions_faq.html). While NBER officially dates separate recessions beginning in 1980 and 1981, we consider them as one economic event given the short period of recovery between them. According to NBER, the recessions began in 1980 Q1, 1981 Q3, 1990 Q3, 2001 Q1, and 2007 Q4. Because of data constraints, we use end-of-year HCM and IUR data for the 1980 and 1990 recessions, and quarterly data for the 2001 and 2007 recessions. We categorized a state as a "borrowing" state if it had an unpaid end-of-year loan balance to the federal government during the business cycle starting with each recession. Additional states that we do not categorize as a borrower may have received cash flow loans that they repaid during the same calendar year as long as they had a zero loan balance at the end of the year.

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## UI Taxation Levels Have Declined Since the 1970s

Declining UI trust fund reserves in recent decades suggest that states have reduced UI tax contribution levels, increased or broadened benefits, or both, although most of the evidence suggests that many states have reduced tax levels gradually. Although there are fluctuations, UI tax contributions as a percentage of UI-covered wages have trended downward in recent decades, from an annual national average of 1.15 percent (1979 to 1988) to 0.79 percent (1989 to 1998) and in the past decade to 0.65 percent (1999 to 2008) (see fig. 2). Contribution rates exceeded 1.0 percent of total wages for each year from 1979 to 1987 but have fallen below that level each year since. Over the same 30-year period, average annual benefits slightly exceeded contributions, with benefits averaging 0.90 percent of annual wages and contributions averaging 0.86 percent of wages. Year-end net trust fund reserves over the period fell from 0.91 percent of wages in 1979 to 0.60 percent in 2008, with further declines in 2009. While there were expected fluctuations around the business cycles, with benefits surging during recessions and contributions rising once the economy strengthens, there has been a general downward trend in contribution rates over the period.

**Figure 2: UI Contributions, Benefits, and Net Reserves, 1979-2008**



Sources: Unemployment Insurance Financial Data Handbook; Employment and Training Administration, Department of Labor.

Note: For more detailed data, see table 8 in app. IV.

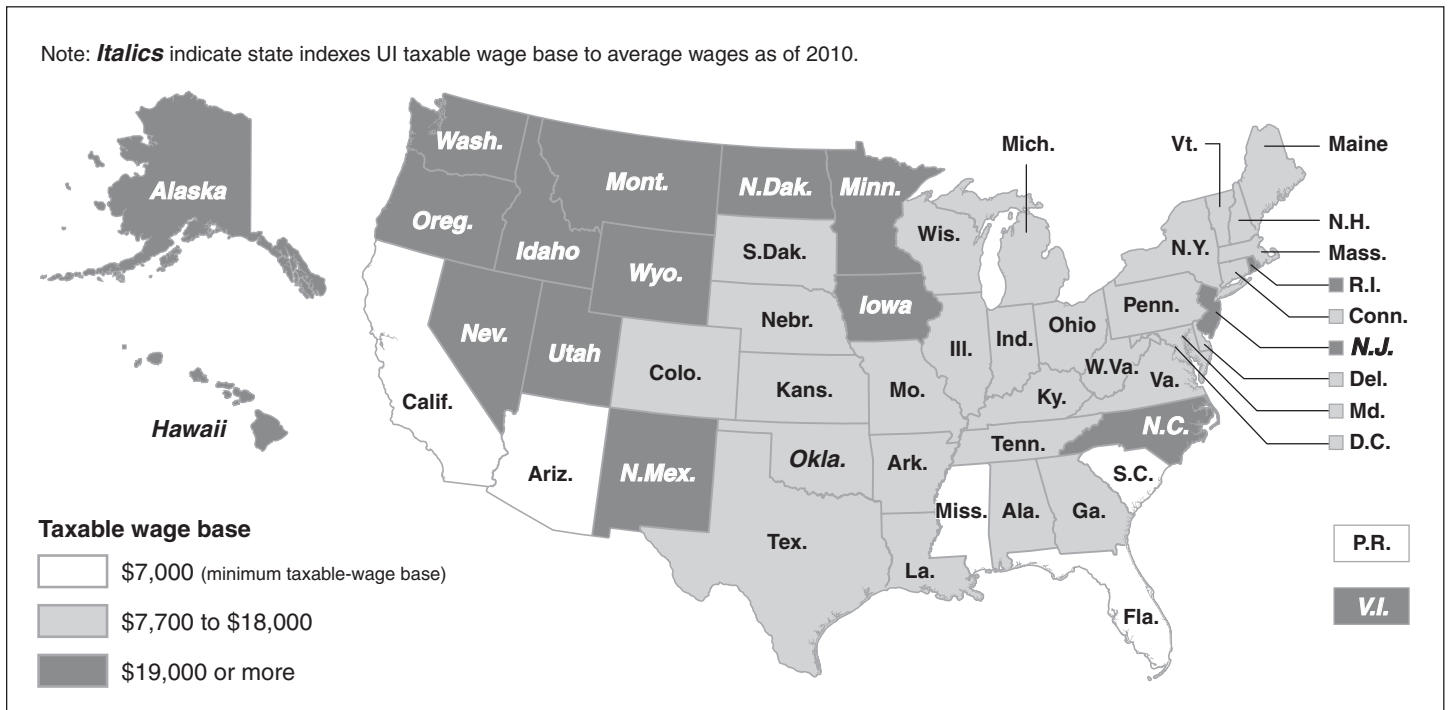
- *Eroding Taxable Wage Bases*

One key reason for falling UI contribution rates is that most states do not index their taxable wage bases, the annual earnings per employee on which employers pay UI taxes, to average wages. As of 2010, only 17 of the 53 state trust funds have taxable wage bases that are indexed to average wages (see fig. 3).<sup>36</sup> In contrast, other states change their wage bases sporadically or very infrequently. Twenty-six have UI taxable wage bases of \$10,000 per worker per year or less, including 6 that have set theirs at the FUTA wage base level of \$7,000 since it last changed in 1983. As a result, employers have paid taxes on a gradually shrinking portion of total wages as wages have risen since then. The ratio of UI-taxable to total

<sup>36</sup>Some states have indexed their taxable wage base for only certain years from 1979 to 2010; others have raised and lowered their bases, without indexing. We categorize states as indexing their wage base if the base in a particular year exceeded the FUTA tax base and is adjusted based on changes in average wages in the state.

wages measured 47.2 percent in 1979 but has declined steadily since then measuring 26.8 percent in 2008. States not indexing their wage bases account for most of this decline—the ratio in these states fell from 0.50 to 0.25 over this period while indexing states’ average ratio dropped only from 0.59 to 0.53 (see fig. 4).

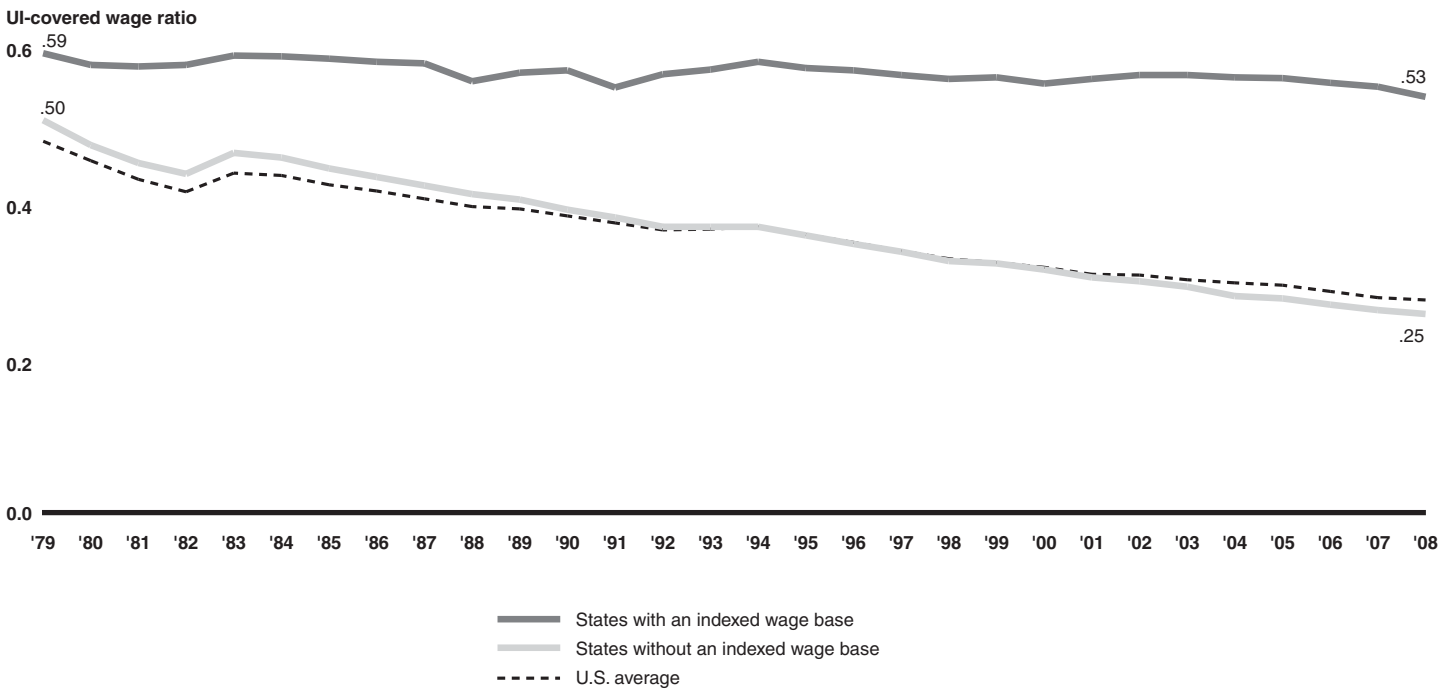
**Figure 3: UI Taxable Wage Bases, 2010**



Source: Employment and Training Administration, Department of Labor.

Note: Each state’s taxable wage base is the annual earnings per employee on which employers pay UI taxes. For other major characteristics of state UI programs, see app. III.

**Figure 4: Comparison of UI-taxable/total Wage Ratio, States with Indexed Taxable Wage Bases vs. Other States, 1979-2008**



Source: GAO calculations based on data from Unemployment Insurance Financial Data Handbook; Employment and Training Administration, Department of Labor.

Note: The UI-taxable/total wage ratio divides the portion of total wages among employees in UI-covered employment each state subjects to UI taxation by the total wages earned by these employees. Some states have indexed their UI taxable wage bases for only some years during 1979-2008. We categorize Virgin Islands as indexing from 2004-8; Rhode Island from 1980-1998; Wyoming from 1984-2008; Oklahoma from 1986-2008; and North Carolina from 1984-2008. States that indexed their wage bases for the entire period are Alaska, Hawaii, Idaho, Iowa, Minnesota, Montana, Nevada, New Jersey, New Mexico, North Dakota, Oregon, Utah, and Washington. For more detailed data, see table 9 in app. IV.

A comparison of financial measures for states that index their UI taxable wage bases and those that do not reveals that indexing states have maintained higher annual average reserve ratios and had many fewer instances of trust fund insolvency, even accounting for the smaller number of states that index (see table 4). In indexing states, employers pay higher contribution rates—paying, on average, lower tax rates on higher tax bases. Benefits in indexing states, as a percentage of annual wages, also exceed those in non-indexing states. Finally, states currently indexing their taxable wage bases have higher trust fund reserve ratios (as of third quarter 2009), although 6 of 17 indexing states currently have outstanding loans (as opposed to those in 25 of the 36 non-indexing states).



**Table 4: UI Financial Statistics, States with Indexed Taxable Wage Bases vs. Other States, 1979-2008**

	Avg. taxable wage base (\$/worker/year)	2010 Avg. taxable wage base (\$/worker/year)	Taxable wages (% of UI-covered wages)	Net reserves (% of UI-covered wages)	Instances of states receiving federal UI loans <sup>b</sup>	UI contributions (% of UI-covered wages)	Tax rate (% of taxable wage base)	Benefits (% of UI-covered wages)	Trust fund balance as of 4th quarter 2009 (% of UI-covered wages)
Indexing states (17, as of 2010) <sup>a</sup>	\$16,112	\$27,218	56.1	2.12	11	1.11	1.96	1.09	1.05
Non-indexing states (36)	\$8,016	\$9,742	36.1	1.44	55	0.84	2.30	0.87	0.37

Source: GAO calculations using data from Unemployment Insurance Financial Data Handbook, ETA.

Note: Figures are annual averages for 1979-2008 except as noted.

<sup>a</sup>See note in figure 4 about states that have indexed their taxable wage base for part of this sample period.

<sup>b</sup>Counts the number of states that had an end-of-year UI loan balance from the federal government during or following each of the four recessions occurring from 1979 to 2008, with consecutive multi-year balances during one recession or recovery counting as one event.

- *Low State UI Tax Rates*

While taxable wage bases have eroded in most states over the last 30 years, the tax rates employers pay on these bases have not offset this decline, according to analysis by the Urban Institute. Table 5 illustrates how minimum tax rates have generally trended downward, while maximums have moved up during the last 30 years. From 1978 to 2008, average minimum tax rates levied on employers by states dropped from 1.14 percent to 0.37 percent of taxable wages. State minimum rates generally moved downward, with the number of states with a minimum rate of zero rose from 3 to 9. The average maximum rate increased from 4.44 percent of taxable wages in 1978 to 7.06 percent in 2008, but most of this jump occurred following a 1982 statutory change raising the state maximum rate required to qualify for the FUTA tax credit from at least 2.7 percent to at least 5.4 percent of taxable wages – since 1988, average maximum tax rates have remained near 7.0 percent while average minimum rates have fallen by half.<sup>37</sup> Maximum statutory tax rates in 2009

<sup>37</sup>In 1982, Pub. L. No. 97-248 §271(c) amended 26 U.S.C. § 3302(b), increasing the state maximum rate to 5.4 percent effective in 1985.

ranged greatly across states, from 5.4 percent of taxable wages per employee in 16 states to 13.2 percent in Pennsylvania.<sup>38</sup> Overall, UI statutory tax rates applied to wage bases averaged 2.7 percent of taxable wages from 1979 to 1988, then 2.2 percent from 1989 to 1998 and again from 1999 to 2008.

**Table 5: Distribution of Minimum and Maximum Statutory UI Tax Rates by State, 1978 to 2008**

Year	Number of states with minimum tax rates of:								Average. minimum rate
	0	0.01 to 0.29%	0.3 to 0.69%	0.7 to 1.09%	1.1 to 1.59%	1.6 to 2.09%	2.1 to 2.59%	2.6% and above	
1978	3	9	11	4	10	2	3	9	1.14
1988	4	11	14	7	7	6	2	0	0.74
1998	8	19	13	2	4	4	1	0	0.50
2008	9	19	14	3	5	1	0	0	0.37

Year	Number of states with maximum tax rates of:								Average. maximum rate
	2.7%	2.71 to 4.0%	4.01 to 5.39%	5.4%	5.41 to 6.49%	6.5 to 7.49%	7.5 to 9.09%	9.1% and above	
1978	4	20	16	1	6	2	2	0	4.44
1988	0	0	0	17	9	5	11	9	6.99
1998	0	0	0	16	10	8	12	5	6.82
2008	0	0	0	17	10	5	8	11	7.06

Source: Urban Institute analysis of ETA "Significant Provisions of State UI Laws," and "Comparison of State Unemployment Insurance Laws," various issues. State averages are simple averages of 51 programs that weight each state equally regardless of size. Data exclude Puerto Rico and the Virgin Islands.

Further, average tax rates on total wages in many states have fallen below what DOL considers to be adequate to cover the costs of benefits.<sup>39</sup> A 2009

<sup>38</sup>To ensure that all employers receive the maximum credit of 5.4 percent against the Federal payroll tax, all state laws provide for assignment of a contribution rate of 5.4 percent or higher. Present federal law permits reduced rates for newly subject employers or employers with at least 1 year of experience with unemployment or other factors bearing a direct relation to unemployment risk. As noted in our 2006 report, the actual maximum tax rate in a state can change from 1 year to the next, because of the use of different schedules or changes in factors used to calculate a tax rate by formula. For example, Massachusetts state law caps its maximum tax rate at 15.4 percent, but, as of July 2009, see the state had set the maximum rate at 12.27 percent. For more information, see GAO, *Unemployment Insurance: States' Tax Financing Systems Allow Costs to Be Shared among Industries*, GAO-06-769 (Washington, D.C.: July 2006).

<sup>39</sup>DOL calculates a state's adequate financing rate by estimating the tax rate that would be charged to all employers if there were no experience rating. They assume the rate is equal to the amount needed to cover benefit payments plus a solvency amount (based on what a state would need to have in its trust fund to achieve an AHCM of 1).

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DOL report on state tax systems reported that all but six states levied average tax rates below the rate adequate to cover benefits and maintain solvency.<sup>40</sup> Similarly, only seven states met their adequate financing rates in 2008; states were better at meeting their adequate financing rates in 2006 and 2007.<sup>41</sup> As of 2009, 20 of 43 states and territories that submitted information for a 2009 DOL report on state tax systems had trust funds with minimum tax rates that were less than \$15 per employee per year, and 12 of these states had a minimum tax rate of zero. In 34 of these 43 states, over half of the employers paid UI tax rates of 0.5 percent or less of total wages, while nationally in the aggregate 67 percent of U.S. employers paid this low rate. In 30 states, as well as the United States overall, this low rate was applied to at least half of the total UI-eligible wages. The United States as a whole only had 3 percent of its employers paying taxes greater than 2 percent of total wages.

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## Benefits Have Remained Fairly Flat in Recent Decades

By several measures UI benefits have remained relatively flat or declined in recent decades, suggesting that declining trust fund reserves cannot be explained by a significant change in benefits. Aggregate annual benefits nationwide averaged 1.10 percent of UI-covered wages from 1979 to 1988, then dropped 0.84 percent from 1989 to 1998 and again to 0.76 percent from 1999 to 2008. Average weekly benefits paid as a percentage of average weekly wages have remained relatively flat from 1979 to 2008, fluctuating from approximately 33 to 38 percent. Measured in terms of replacement rates, or the ratio of individual benefits received to prior wages, benefits to wages have also remained fairly flat from 1988 to 2007, ranging from 44 to 47 percent. Moreover, as we found in 2007, the UI reciprocity rate, which effectively measures the percentage of the unemployed who receive benefits, gradually declined from the 1950s through the 1980s and remains below the near-50 percent rate of the 1950s. In 1979, the ratio of the insured unemployment rate to the total unemployment rate measured 48 percent, compared to 43 percent in 2008.<sup>42</sup> Further, low-wage and part-time workers continue to experience

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<sup>40</sup>See U.S. Department of Labor, Office of Workforce Security, Division of Fiscal and Actuarial Services, *2009: Significant Measures of State UI Tax Systems* (December 2009).

<sup>41</sup>The states who met or exceeded their adequate financing rates from 2006-2009 were Maine, Mississippi, Montana, and New Mexico.

<sup>42</sup>The insured unemployment rate is calculated in terms of UI-covered employment, while the total unemployment rate is calculated as a percentage of the labor force.

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low rates of benefit receipt.<sup>43</sup> For example, we found that low-wage workers were more than twice as likely to be unemployed, but about half as likely to receive UI benefits.<sup>44</sup> We have also found that past declines in the percentage of unemployed who receive UI benefits are associated with declines in state UI trust fund financial conditions. For example, in 1993 we found that if the same proportion of unemployed workers had received comparable benefit payments during the 1990-91 recession as during the 1974-75 recession, about \$20 billion more in unemployment benefits would have been available to stabilize the economy and maintain the incomes of the unemployed. In addition, we found that states with declining or insolvent trust funds were likely to make it more difficult for unemployed workers to qualify for benefits and to reduce the portion of wages of former workers replaced by unemployment benefits.<sup>45</sup>

In addition to paying regular benefits, states are also typically responsible for funding a portion of benefits paid under the federal-state Extended Benefits program (EB). While states fund approximately half of the cost of EB, the aggregate cost of these benefits for the states represents a small portion of total benefits paid by the states. From 1979 to the third quarter of 2009, EB payments totaled \$13.3 billion, approximately \$4.8 billion of which the states paid for. These amounts represent 1.9 percent of total benefits paid, and 0.7 percent of state benefits paid, and hence have had relatively little impact on state trust funds. Given the surge in EB in 2009, with over \$4 billion in total through the third quarter, without the federal

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<sup>43</sup>According to our 2007 report, there is some evidence that the general decline in UI since the 1950s is partly explained by the reduction in union employment—making workers less aware of benefits—and the migration of manufacturing from high-benefit states to low-benefit states—making applying for benefits less remunerative. For more information, see GAO, *Unemployment Insurance: Low-Wage and Part-Time Workers Continue to Experience Low Rates of Receipt*, [GAO-07-1147](#) (Washington, D.C.: Sept. 7, 2007).

<sup>44</sup>States administer UI re-employment services to help claimants obtain employment before exhausting UI benefits. These services can impact UI trust fund levels by reducing the number of weeks claimants receive benefits. See GAO, *Unemployment Insurance: More Guidance and Evaluation of Worker-Profiling Initiative Could Help Improve State Efforts*, [GAO-07-680](#) (Washington, D.C.: June 2007); *Unemployment Insurance: Enhancing Program Performance by Focusing on Improper Payments and Reemployment Services*, [GAO-06-696T](#) (Washington, D.C.: May 4, 2006); *Unemployment Insurance: Factors Associated with Benefit Receipt and Linkages with Reemployment Services for Claimants*, [GAO-06-484T](#) (Washington, D.C.: Mar. 15, 2006); and *Unemployment Insurance: Better Data Needed to Assess Reemployment Services to Claimants*, [GAO-05-413](#) (Washington, D.C.: June 2005).

<sup>45</sup>See [GAO/HRD-88-55](#) and GAO, *Unemployment Insurance: Program's Ability to Meet Objectives Jeopardized*, [GAO/HRD-93-107](#) (Washington, D.C.: Sept. 28, 1993).

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government funding 100 percent of most EB costs from February 17, 2009, through April 5, 2010, under ARRA, as amended, the impact would have been much greater; it remains to be seen if EB becomes a significant burden on states later in 2010.<sup>46</sup>

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### States Annually Adjust Tax Rates Based on Trust Fund Levels

Currently, all states adjust UI tax rates yearly, based on an annual measurement of the size of the trust fund and calculation of employer experience rating. Generally, states raise UI tax rates as the trust fund diminishes in order to try to replenish the fund and lower them when the fund grows to a certain level. This practice has the advantage of providing automatic stabilization to UI funding. However, it creates two problems. First, annual adjustments might allow rates to remain inappropriately high or low for up to an entire year if economic conditions change sharply soon after the “fund trigger date” on which a state measures its trust fund. Some states told us that this occurred during the recent recession, which began in late 2007, and worsened in fall 2008 following the financial meltdown, right after some states had measured their trust funds. If states adjusted their tax rates more frequently, employers may have seen more gradual rate increases instead of the widespread sharp increases going into effect in 2010. Second, tying tax rates to trust fund conditions means that states are likely to raise taxes on employers when economic and labor market conditions are weak (coinciding with increased benefit payouts and low trust funds). Higher taxes during weak economic times may exacerbate labor market conditions (since higher UI taxes make it more expensive to hire workers) and economic recovery in general. Thus, the effects of state tax adjustments erode at least some of the stabilizing macroeconomic effects of paying UI benefits.

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### Among Policy Options, Revenue-Related Reforms May Hold Key to Improving UI Trust Fund Solvency

Given the UI program’s vision for economic stabilization through business cycles, it has been a policy goal for at least 3 decades to promote greater forward funding of the individual state funds. In 1980 and 1994 national commissions issued many recommendations for increasing and stabilizing program funding. These commissions, as well as other studies, have encouraged states to build up reserves and reduce the dependence on borrowing during difficult economic times. Based on our current findings, table 6 lists some policy options for improving long-term trust fund financing with some of their advantages and disadvantages.

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<sup>46</sup>Pub. L. No. 111-5, as amended by Pub. L. No. 111-144.

**Table 6: Policy Options for Improving UI Funding**

<b>Policy</b>	<b>Who could implement</b>	<b>Advantages</b>	<b>Disadvantages</b>
Raise and index FUTA taxable wage base	Congress	<p>Would reverse years of erosion of UI tax base and maintain wage base as a consistent proportion of income.</p> <p>Would cause states to raise their taxable wage bases to qualify for FUTA credit.</p> <p>Could allow federal government and states to reduce statutory tax rates for given UI funding goals.</p>	<p>Higher UI taxes could discourage hiring.</p> <p>Federal taxable wage base represents different tax burdens to different states.</p> <p>Resistance of states to increasing burden on employers to pay more to federal trust funds.</p>
Reduce number of employers paying very low UI tax rates	States <sup>a</sup>	<p>Would increase UI contributions.</p> <p>Would better distribute costs of social insurance.</p>	<p>Fairness—UI taxes may not reflect costs attributable to employers.</p> <p>Would reduced incentive for employers to avoid layoffs.</p>
Reduce large tax subsidies across employers and industries	States <sup>a</sup>	<p>Distribution of UI taxes based on costs created by employer layoffs.</p> <p>Stronger incentives for employers to avoid layoffs.</p>	<p>Increased rates may encourage employers with high tax rates to try to circumvent tax.</p>
Adjust state tax rates more frequently than annually and raise solvency targets before implementing lower tax rates	States <sup>a</sup>	<p>Tax rates could adjust before trust fund becomes severely depleted.</p> <p>More funds raised during strong, not weak, economic conditions.</p>	<p>Higher administrative costs.</p> <p>Less ability of employers to anticipate tax rates.</p> <p>Resistance from employers to paying relatively high UI taxes when trust funds were flush.</p>
Set additional conditions on interest-free loans	Department of Labor <sup>b</sup>	<p>Strengthen incentives for states to avoid loans with more robust forward funding.</p>	<p>Increased reliance on higher tax rates during difficult economic times.</p> <p>Estimated small impact.</p> <p>State objections to paying more for funds their taxes provide.</p>
Offer increased interest credits to state trust funds funded above a certain level	Congress	<p>Incentive for states to save more in trust funds.</p>	<p>States with lower funding balances may receive less in interest.</p>

Source: GAO analysis based on findings.

<sup>a</sup>While only states could implement these policy changes, Congress could include these as requirements for employers in a state to qualify for the FUTA tax credit.

<sup>b</sup>Labor has published proposed rules on interest-free loan conditions that have yet to be finalized. See footnotes 20 and 51 for additional information on this proposed rule.

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- *Raise and index FUTA taxable wage base*

The FUTA taxable wage base has remained fixed at \$7,000 per worker per year since 1983.<sup>47</sup> Six state trust funds have also kept their taxable wage base at that level since then, while an additional 20 set theirs between \$7,000 and \$10,000. From 1983 to 2008, the average weekly wage in UI-covered employment rose from \$336 to \$869 per worker, a rise of 159 percent. By keeping the wage base fixed instead of rising with wages, the percentage of wages subject to UI taxation has fallen from 43.1 percent in 1983 to 26.8 percent in 2008. This means that a steadily shrinking portion of the wage distribution is responsible for raising UI revenues. This also suggests that any impact UI taxes have on reducing wages has been borne increasingly by lower-income workers. Raising the FUTA base to make up for some of the relative erosion in the UI revenue base and indexing it to future wage growth would ensure that a more constant share of total income supports the UI program. If the FUTA taxable wage base had risen roughly with the changes in wages since 1983, the 2008 taxable wage would be approximately \$18,100—higher than the 2010 tax bases for all but 17 state trust funds.<sup>48</sup> Since employers in states with tax bases which are less than the FUTA tax base would not be eligible for the full tax credit, states would almost certainly raise and index theirs to the new, higher FUTA tax base. The one-time increase and indexing of the taxable wage base would mean that state UI tax revenue would more likely represent a consistent share of total wages, as well as spread the effective tax incidence of UI taxes across more of the wage distribution. It would also allow states to set lower tax rates in order to raise a given amount of revenue, which is generally a more efficient way to tax than to set higher tax rates on a narrower tax base.

Most state UI program officials we interviewed said they would welcome, or at least accept, a higher FUTA taxable wage base, some emphasizing that some states have not been able to raise taxable wage bases on their own. Other representatives said they would object to higher federal UI taxes, some citing instances when the federal government raised the statutory ceiling that triggers a Reed Act distribution, thus postponing the

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<sup>47</sup>For comparison, the taxable wage base for contributions to Social Security, which is indexed to average wages, rose from \$35,700 per worker per year in 1983 to \$102,000 in 2008, an increase of 186 percent.

<sup>48</sup>This calculation does not correct for any changes in the wage distribution since 1983 that might affect the relationship between the taxable wage base and total UI revenue collected each year.

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payment of money to state trust funds. Higher UI taxes, by making employment somewhat more expensive, could discourage some employers from hiring; however, the federal government could lower the effective 0.8 percent tax rate states have paid since 1985, which would reduce the impact of raising and indexing the FUTA tax base.

- *Reform UI tax rates structure*

Another set of policy options would involve adjusting the UI tax rates employers pay. For example, states could act to (1) reduce the number of employers paying very low UI tax rates; (2) reduce large subsidies among employers and industries that pay less in UI taxes than benefits paid to their former workers; (3) adjust tax rates more frequently; and (4) set taxes to raise more funds during strong economic times. The first option would widen the effective revenue base for the program by getting contributions from more employers and allow the state to reduce tax rates for the higher levels of the tax schedule. There are distinct arguments in favor of, and against, setting minimum tax rates for all employers, and experience rating in general. Assigning higher tax rates to employers who lay more workers off distributes program costs in an arguably fair way and creates an incentive for employers to retain workers during difficult economic times. On the other hand, all employers, even those without a history of layoffs, face uncertainty about the future UI claims of their employees, an argument for every employer paying to cover this social insurance.

As a second option, states could adjust experience ratings to reduce significant subsidies for some employers and industries. GAO reported in 2006 that industries with more seasonal layoffs, such as construction and agriculture, tend to pay less in UI contributions than their workers receive in benefits.<sup>49</sup> Such experience rating reform could raise additional revenues from high-layoff employers whose tax rates hit tax rate maximums, better distribute the UI tax burden to those employers who create higher benefit costs through layoffs, and reduce benefit costs to the extent that higher tax rates discourage these employers from laying workers off in the first place. On the other hand, raising the rates charged

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<sup>49</sup>For more on experience rating and the impact on UI tax rates, see GAO, *Unemployment Insurance: States' Tax Financing Systems Allow Costs to Be Shared among Industries*, [GAO-06-769](#) (Washington, D.C.: July 2006).



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to employers with the highest experience rating might create strong incentives for firms to circumvent paying UI taxes.<sup>50</sup>

A third option would encourage states to adjust UI tax rates more frequently if trust fund conditions change significantly and to raise more revenues when economic conditions are stronger. Annual adjustments to tax rates can lead to sharp increases when labor markets are weak. More frequent, even twice-yearly, measurement of trust fund conditions and tax rate adjustments could allow employers to absorb changes in tax burden more gradually. However, more frequent tax adjustments could create more administrative costs to implement, and employers may not like the increased uncertainty caused by more frequent tax adjustments. In order to build up more of a funding cushion when economic conditions are strong rather than when they are weak, states could consider setting higher trust fund targets before lowering tax rates. However, this would require employers tolerating higher UI tax rates than under the current system when trust funds are relatively flush.

- *Set additional loan conditions while increasing credits on trust fund balances*

Recent proposed rules by Labor would seek to define eligibility for interest-free terms on federal UI loans by setting standards states would have to meet for maintaining the levels of their trust funds or a level of tax

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<sup>50</sup>These efforts might include challenging laid off employees' eligibility to receive benefits, trying to get a new experience rating by changing the identity of the company (perhaps through a sham sale or new name), or declaring that a firm's employees are independent contractors and therefore outside the UI system. See GAO, *Unemployment Insurance: Survey of State Administrators and Contacts with Companies Promoting Tax Avoidance Practices*, [GAO-03-819T](#) (Washington D.C.: June 19, 2003), for more on this issue.

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“effort” in the years prior to applying for a loan.<sup>51</sup> While loans clearly serve a vital function in financing benefits during difficult economic times, they somewhat reduce the incentive for states to maintain robust trust funds. Stricter interest-free loan qualifications might encourage states to maintain higher funding targets, although Labor estimates such effects to be small. However, reducing access to interest-free loans could lead states to rely more heavily on raising tax rates when UI trust funds fall close to zero, which likely coincides with difficult economic periods when labor markets might benefit from lower, not higher, taxes. States may object to being charged more to take out loans, particularly during a recession as severe as the most recent one; in interviews, some state representatives expressed a sentiment that the states fund the federal trust funds that provide loans when states need them, and therefore they should be available interest free. At the same time that rules could restrict interest-free loans, paying higher rates of interest on trust fund balances above a certain level (say, on balances corresponding to an AHCM of 1.0 or higher) could provide a positive incentive for states to accumulate more in UI reserves; for a given amount of interest, this would mean that states with lower funding levels would receive lower rates of interest.

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## Conclusions

Like UI funding itself, interest in the financial condition of state UI trust funds seems to follow the business cycle: during recessions that drain reserves and force states to borrow to pay benefits, UI stakeholders focus on the potential to improve forward funding in the future. But when the economy, and with it trust fund levels, recovers, the urgency to do so subsides. As it stands today, the long-term decline of UI funding, culminating in widespread borrowing by state trust funds and the dire

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<sup>51</sup>42 U.S.C. § 1322(b)(2)(C). In the preamble to its proposed regulations Labor described three approaches it considered involving both solvency and tax effort criteria states would have to meet in order to qualify for interest-free “cash flow” advances. In one approach, a state would need to maintain an AHCM of 1.0 in at least 1 of the 5 years prior to obtaining a loan and, for each year between the last year in which the solvency goal was met and the year of the potential loan, need to collect unemployment taxes (measured as a percentage of total wages) of at least 80 percent of the prior year’s rate; and the tax rate would have to be at least as high as 75 percent of the percentage of benefits paid out. A second approach would set only the solvency requirement, not the tax effort condition, and a third approach would define the solvency standard as a reserve ratio of 1.7 percent instead of an AHCM of 1.0. After reviewing all three approaches, DOL selected the first one to include in its proposed rule. See Employment and Training Administration, 20 CFR Part 606, “Federal-State Unemployment Compensation (UC) Program; Funding Goals for Interest-Free Advances; Proposed Rule,” 74 Fed. Reg. 30,402 (June 25, 2009). DOL officials told us that they plan to issue a final rule in June 2010, but may not implement the rule for a few years.

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financial condition of the program, raises critical questions about the ability of the program to function as it has in the past.

To be sure, no one would argue that forward funding implies that a state should never have to borrow to pay benefits. Further, the program is designed to allow states significant latitude in deciding how much (and how) to tax their employers and how much to pay in benefits. Further, a lack of consistent standards for trust fund “adequacy” and the decentralization of UI policy make it understandable, and to some parties even desirable, that forward funding of trust funds varies across states and over time.

Nevertheless, Labor’s prognosis for the ability of borrowing states to repay their loans to avoid employer tax penalties is not optimistic. States are responding to low trust fund levels by raising tax rates on employers, which could undermine recovery. Meanwhile, any increased borrowing could change the nature of the program’s federal-state partnership, with the federal government taking on more chronic funding responsibility for paying benefits rather than providing, as originally envisioned, a backstop to states when they experience financial emergencies. Weakening forward funding could put pressure on states to reduce benefits, which might compromise the program’s goal of providing macroeconomic stability during recessions.

Now is the time, therefore, to consider changes to federal program policies that could better assure the long-term financial structure of UI trust funds. The fact that states with an indexed taxable wage base have a better record for maintaining solvency and in some cases weathering high unemployment suggests one direction that federal policymakers might take to preserve the program without compromising state needs for flexibility.

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## Matter for Congressional Consideration

To provide incentives for states to build up and maintain stronger UI trust fund reserves, the Congress should begin to consider raising the FUTA taxable wage base from its current level of \$7,000 and indexing this base to average annual wages. At the same time, the Congress should consider measures to ameliorate the potential increase in the tax burden on employers, such as lowering the FUTA statutory tax rate or increasing the FUTA tax credit. Enacting such measures to take effect when the current economic situation improves would create more robust funding in the future by encouraging states to broaden the revenue base for UI funding and maintain a consistent base relative to wages.

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## Agency Comments

We provided a draft of this report to the Department of Labor, which provided written comments. Labor generally agreed with the findings and conclusions of our report. Labor said that the report is both important and timely considering the serious risk facing the financing of state UI benefits, which is putting at risk the ability of the UI system to act as an effective stabilizer for the economy and may result in many states reducing their UI benefit levels. While concurring with the report's emphasis on the value of UI forward funding, Labor added that there may be additional options to address solvency concerns, including greater federal cost sharing such as full federal funding of extended benefits and various reinsurance models. It also said that complex relationships between solvency, tax effort, and differences in benefit adequacy need to be more deeply addressed. In response to this comment, we revised the report to provide more information from our prior work on the relationship between states' UI financial condition and reductions in benefit levels, although we did no new analysis beyond what we present here. Labor also said, with respect to one of our policy suggestions, that having state tax rate adjustments occur more frequently may be inconsistent with improving long-term trust fund financing. We agree that the common practice of adjusting rates upward in response to lower trust fund reserves, regardless of frequency, is inconsistent with forward funding principles; we include among our policy options that states change their tax structures to raise more revenues during strong, rather than weak, economic periods. However, given the mechanism of tying tax rates to trust fund levels, we still believe that more frequent adjustments may allow states to change rates to raise more revenues before trust fund conditions become severe and sharp rate increases are required. Labor's comments appear in appendix V. Labor also provided technical comments that we incorporated as appropriate.

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As agreed with your offices, unless you publicly announce its contents earlier, we plan no further distribution until 30 days after the date of this letter. At that time, we will send copies of this report to the Secretary of Labor, appropriate congressional committees, and other interested parties. We will also make copies available to others on request. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

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If you have any questions concerning this report, please contact Andrew Sherrill at (202) 512-7215. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made contributions are listed in appendix VI.

Sincerely yours,



Andrew Sherrill  
Director, Education, Workforce,  
and Income Security Issues

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# Appendix I: Objectives, Scope, and Methodology

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The objectives of this report were to (1) describe the current condition of state UI trust funds, (2) highlight the policies or practices that have contributed to their conditions, and (3) identify options for improving state forward funding in the future to better ensure the solvency of the UI program.

To address the first and second objectives, we analyzed UI state statistical data on current unemployment insurance financial conditions and current program information from the Department of Labor's Employment and Training Administration (ETA). We also used historical data from ETA to compare the program's current and recent finances to that of past years and to research causes of the current financial problems. We also reviewed applicable federal and state laws, regulations and guidance, and relied on data and reports by the Bureau of Labor Statistics, Labor, the Congressional Budget Office, the Congressional Research Service, states' workforce agencies and related associations, and other UI advocacy and policy groups. We supplemented our analysis with interviews with officials from some of these organizations. In particular, we conducted in-depth interviews with UI program officials from a sample of ten states that represent a range of geographic locations, economic conditions, and UI trust fund reserve levels. These ten states were Alaska, California, Georgia, Maine, Michigan, New York, Oregon, Texas, Utah, and Washington. We also reviewed UI governing state and federal legislation, regulations, and guidance. We determined that the data we used for our analysis were sufficiently reliable to address our key objectives. A consultant, an expert in UI financing, also performed analysis of state trust funds on our behalf.

To address the last objective, we synthesized conclusions from our statistical analysis of state and national UI program data. We pose potential advantages and disadvantages of proposed policy options derived from our interviews with state UI program officials and with other policy experts. We also reviewed past conclusions and recommendations in reports by GAO, DOL, CBO, CRS, four past government advisory councils on unemployment compensation, and public policy organizations.

We conducted this performance audit from May 2009 through April 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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# Appendix II: Unemployment Insurance Measures in the American Recovery and Reinvestment Act

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The American Recovery and Reinvestment Act of 2009 (ARRA) contains several provisions to expand and extend unemployment compensation.<sup>1</sup> The law

- extended the Emergency Unemployment Compensation program of 2008 (EUC) through December 31, 2009;
- increased weekly benefits by \$25 per week, temporarily funded by federal money;
- provided up to \$7 billion total in “modernization incentive payments” to states whose UI rules contain specific provisions that broaden benefit eligibility;
- waived interest due on Title XII loans through December 31, 2010;
- provided for the federal government to pay 100 percent, instead of 50 percent, of the costs of extended benefits payments (EB)<sup>2</sup>;
- exempted the first \$2,400 of unemployment benefits received by individuals from tax in 2009; and
- provided \$500 million total to states for additional administrative costs.

ETA reports that, as of March 26, 2010, total obligations for EUC payments for extended benefits equaled \$37.2 billion and for the additional \$25 weekly benefit obligations totaled \$12.1 billion; \$2.8 billion in modernization payments have been distributed to 31 states and the District of Columbia; \$6.5 billion for payments to states to cover their portion of EB payments; and the \$500 million distribution to states for administrative expenses.

Each state’s potential modernization incentive grant is proportional to its FUTA taxable wages, payable in two installments. To receive the first grant, for one-third of the total available to each state, state law must

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<sup>1</sup>Pub. L. No. 111-5.

<sup>2</sup>Congress extended EUC, increased weekly benefits, and full funding of EB through February 28, 2010 (Department of Defense Appropriations Act, 2010 Pub. L. No. 111-118, December 19, 2009) and then enacted another extension through April 5, 2010 (Temporary Extension Act of 2010, Pub. L. No. 111-144, Mar. 2, 2010).

provide for either a base period that uses recent wages or an alternative base period using recent wages. Specifically, the regular base period must include the most recently completed calendar quarter before the start of the benefit year, or if the claimant cannot meet monetary qualifying requirements using a regular base period that excludes this quarter, the alternative base period must include the most recently completed calendar quarter.

If a state qualifies under this provision, it may receive the remaining two-thirds if its eligibility rules include two of four possible criteria. These criteria are:

1. UI benefits are payable to certain individuals seeking only part-time work.
2. An individual is not disqualified from UI for separations due to certain compelling family reasons.
3. An additional 26 weeks of benefits is paid to exhaustees who are enrolled in and making satisfactory progress in certain training programs.
4. Dependents' allowances of at least \$15 per dependent per week, subject to a minimum aggregation, are paid to eligible beneficiaries.

As of March 26, 2010, 31 states and the District of Columbia have qualified for \$2.8 billion in grants, including 22 that have received full payments (see fig. 5). The Department of Labor has appealed to states to apply for the remaining \$4.15 billion in modernization grant funding that remained unclaimed as of that date. Any changes that states make to state unemployment programs as a result of ARRA's modernization provisions must be permanent, and thus could increase funding challenges for states in the future.<sup>3</sup>

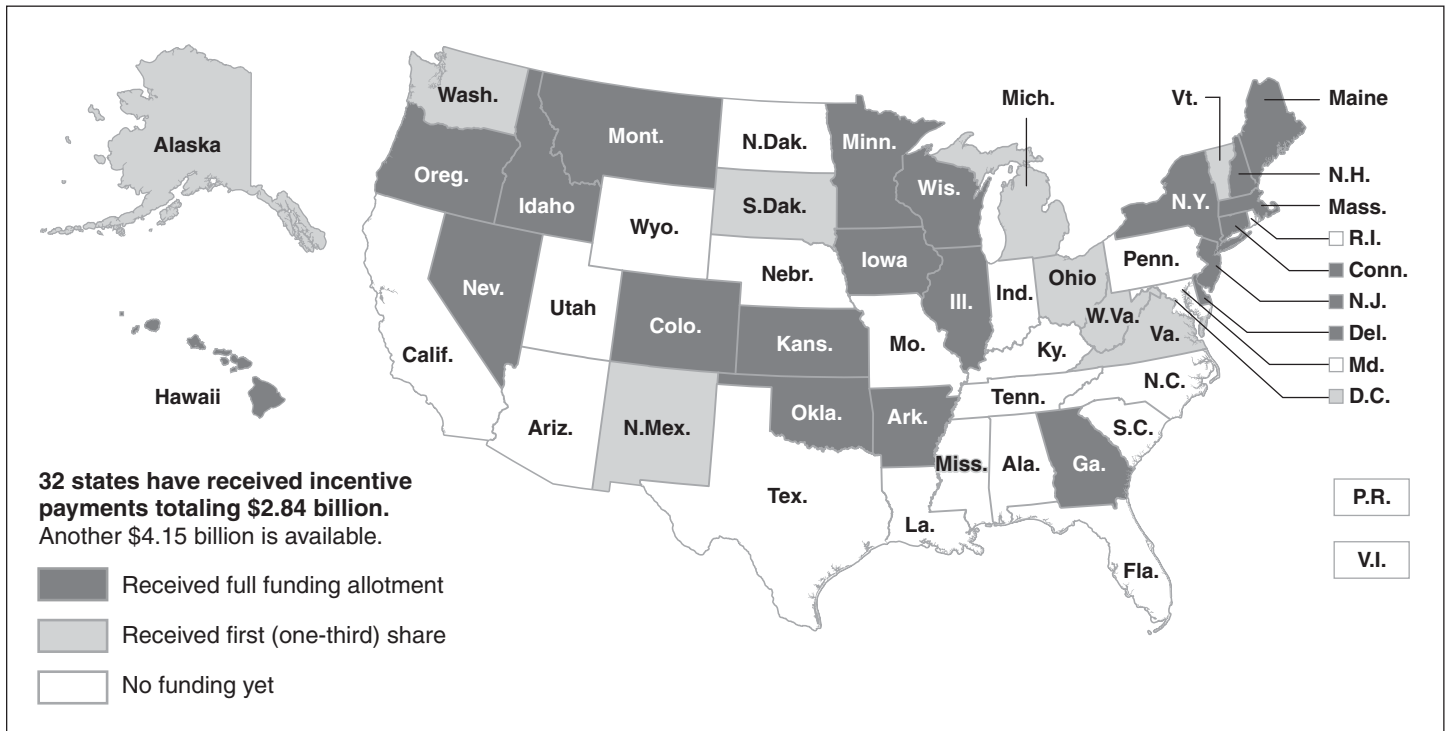
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<sup>3</sup>A state may delay the effective date of a provision to qualify for an incentive payment up to 12 months.



**Appendix II: Unemployment Insurance Measures in the American Recovery and Reinvestment Act**

**Figure 5: Distribution of ARRA UI Modernization Incentive Grants, as of Mar. 26, 2010**



Source: Employment and Training Administration, Department of Labor.

# Appendix III: Major Characteristics of State UI Programs, as of March 2010

State	Weekly benefit formula	Minimum weekly benefit	Maximum weekly benefit	Number of benefit weeks	Minimum payroll size for benefit eligibility	2010 taxable wage base (per worker) (italics = indexed to wages)	2010 minimum & maximum employer tax rates New employer rate
AL	1/26 average of 2 highest quarters	\$45	\$265	15-26	20 weeks or \$1,500 in any quarter	\$8,000	0.44% 6.04% 2.70%
AK	0.9-4.4% of annual wages + \$24 per dependent up to \$72	56-128	370-442	16-26	Any size <sup>a</sup>	<i>34,100</i>	1.00% 5.40% 1.96%
AZ	1/25 high quarter wages	60	240	12-26	20 weeks or 1,500 in any quarter	7,000	0.02% 5.40% 2.00%
AR	1/26 high quarter wages	79	441	9-26	One employee for 10 or more days in a calendar year	12,000	0.90% 6.80% 3.70%
CA	1/23 to 1/26 high quarter wages	40	450	14-26	Over 100 in any quarter	7,000	1.50% 6.20% 3.40%
CO	Higher of 60% of 1/26 of 2 consecutive high quarter wages, capped by 50% of average weekly earnings or 50% of 1/52 base period earnings capped by 55% of average weekly earnings	25	443-487	13-26	20 weeks or 1,500 in any quarter	10,000	0 5.40% 1.70%
CT	1/26 average of 2 highest quarters + \$15 per dependent, up to 5; dependents allowance capped at weekly benefit amount (For construction workers, 1/26 high quarter)	15-30	537-612	26	20 weeks or 1,500 in any quarter	15,000	1.90% 6.80% 3.00%

**Appendix III: Major Characteristics of State  
UI Programs, as of March 2010**

<b>State</b>	<b>Weekly benefit formula</b>	<b>Minimum weekly benefit</b>	<b>Maximum weekly benefit</b>	<b>Number of benefit weeks</b>	<b>Minimum payroll size for benefit eligibility</b>	<b>2010 taxable wage base (per worker) (italics = indexed to wages)</b>	<b>2010 minimum &amp; maximum employer tax rates New employer rate</b>
DE	1/46 total wages in 2 highest quarters	\$20	\$330	24-26	20 weeks or \$1,500 in any quarter	\$10,500	0.10% 8.00% 2.10%
DC	1/26 high quarter wages	50	359	19-26	Any size	9,000	1.30% 6.60% 2.70%
FL	1/26 high quarter wages	32	275	9-26	20 weeks or 1,500 in any quarter	7,000	0.12% 5.40% 2.70%
GA	1/42 of wages in highest 2 quarters or 1/21 high quarter wages	44	330	6-26	20 weeks or 1,500 in any quarter	8,500	0.025% 5.40% 2.62%
HI	1/21 high quarter wages	5	559	26	Any size	<i>38,800</i>	0 5.40% 1.90%
ID	1/26 high quarter wages	72	334	10-26	20 weeks or 1,500 in any quarter	<i>33,300</i>	0.447% 5.40% 1.00%
IL	47% of claimant's average weekly wage in 2 highest quarters	51-77	385-531	26	20 weeks or 1,500 in any quarter	12,520	0.60% 6.80% 3.10%
IN	5% of 1st \$2,000 of wage credits in high quarter, 4% of remaining high quarter wages credits; wage credits limited to \$9,250	50	390	8-26	20 weeks or 1,500 in any quarter	9,500	1.10% 5.60% 2.70%
IA	1/19 – 1/23 high quarter wages for claimants with dependents	56-67	374-459	9-26	20 weeks or 1,500 in any quarter	<i>24,500</i>	0 8.00% 1.00%
KS	4.25% high quarter wages	109	436	10-26	20 weeks or 1,500 in any quarter	8,000	0 7.40% 4.00%
KY	1.3078% base period wages	39	415	15-26	20 weeks or \$1,500 in any quarter	8,000	1.00% 10.00% 2.70%

**Appendix III: Major Characteristics of State  
UI Programs, as of March 2010**

State	Weekly benefit formula	Minimum weekly benefit	Maximum weekly benefit	Number of benefit weeks	Minimum payroll size for benefit eligibility	2010 taxable wage base (per worker) (italics = indexed to wages)	2010 minimum & maximum employer tax rates New employer rate
LA	1/25 of the average of wages in 4 quarters of base period x 1.05 x 1.15	\$10	\$247	26	20 weeks or 1,500 in any quarter	7,700	0.10% 6.20% 2.89%
ME	1/22 average wages paid in 2 highest quarters of base period + \$10 per dependent up to ½ weekly benefit amount	62-93	356-534	22-26	20 weeks or 1,500 in any quarter	12,000	0.44% 5.40% 1.57%
MD	1/24 high quarter wages + \$8 per dependent up to 5 dependents	25-65	410	26	Any size	8,500	0.60% 9.00% 2.20%
MA	50% average weekly wage + \$25 per dependent up to ½ weekly benefit amount	33-49	629-943	10-30	13 weeks or 1,500 in any quarter	14,000	1.26% 12.27% 2.83%
MI	4.1% high quarter wages + \$6 for each dependent up to 5	117-147	362	14-26	20 weeks or 1,000 in calendar year	9,000	0.60% 10.30% 2.70%
MN	Higher of 50% of 1/13 high quarter wages up to 43% of State average weekly wages or 50% of 1/52 base period wages up to 66% of state average weekly wages	38	377-585	11-26	Any size	<i>27,000</i>	0.556% 10.70% 2.3116%
MS	1/26 high quarter wages	30	235	13-26	20 weeks or 1,500 in any quarter	7,000	0.70% 5.40% 2.70%
MO	4.00% of the average of the 2 high quarter wages	35	320	8-26	20 weeks or 1,500 in any quarter	13,000	0.00% 9.75% 3.51%
MT	1% base period wages or 1.9% wages in 2 high quarters	125	422	8-28	\$1,000 in current or preceding year	<i>26,000</i>	0 6.12% 2.70%
NE	½ average weekly wages	30	318	1-26	20 weeks or 1,500 in any quarter	9,000	0 5.40% 1.29%

**Appendix III: Major Characteristics of State  
UI Programs, as of March 2010**

<b>State</b>	<b>Weekly benefit formula</b>	<b>Minimum weekly benefit</b>	<b>Maximum weekly benefit</b>	<b>Number of benefit weeks</b>	<b>Minimum payroll size for benefit eligibility</b>	<b>2010 taxable wage base (per worker) (italics = indexed to wages)</b>	<b>2010 minimum &amp; maximum employer tax rates New employer rate</b>
NV	1/25 high quarter wages	\$16	\$400	12-26	225 in any quarter	<i>27,000</i>	0.25% 5.40% 2.95%
NH	1%-1.1% annual wages	32	427	26	20 weeks or 1,500 in any quarter	10,000	0.10% 6.50% 2.70%
NJ	60% of claimant's average weekly wage + dependents allowance	87-100	600	1-26	1,000 in any year	<i>29,700</i>	0.30% 5.40% 2.6825%
NM	60.0% of average weekly wage paid in base period quarter in which wages were highest	71-106.50	426-526	16-26	20 weeks or 450 in any quarter	<i>20,800</i>	0.03% 5.40% 2.00%
NY	1/26 high quarter wages unless high quarter wages ≤ \$3,575 then, 1/25 high quarter wages	64	405	26	300 in any quarter	8,500	0.70% 8.70% 4.10%
NC	1/26 high quarter wages	43	505	13-26	20 weeks or 1,500 in any quarter	<i>19,700</i>	0 6.84% 1.20%
ND	1/65 of wages in 2 high quarters + 1/2 wages in 3rd high quarter	43	431	12-26	20 weeks or 1,500 in any quarter	<i>24,700</i>	0.20% 9.86% 1.60%
OH	1/2 claimant's average weekly wage + dependents allowance of \$1-\$133 based on claimant's average weekly wage and number of dependents	106	375-508	20-26	20 weeks or 1,500 in any quarter	9,000	0.30% 9.00% 2.70%
OK	1/23 high quarter wages	16	430	18-26	20 weeks or \$1,500 in any quarter	<i>14,900</i>	0.10% 5.50% 1.20%
OR	1.25% base period wages	115	493	3-26	18 weeks or 1,000 in any quarter	<i>32,100</i>	0.90% 5.40% 2.40%

**Appendix III: Major Characteristics of State  
UI Programs, as of March 2010**

<b>State</b>	<b>Weekly benefit formula</b>	<b>Minimum weekly benefit</b>	<b>Maximum weekly benefit</b>	<b>Number of benefit weeks</b>	<b>Minimum payroll size for benefit eligibility</b>	<b>2010 taxable wage base (per worker) (italics = indexed to wages)</b>	<b>2010 minimum &amp; maximum employer tax rates New employer rate</b>
PA	1/23-1/25 high quarter wages + \$5 for 1 dependent; \$3 for 2nd dependent	35-4\$3	\$564-572	16 or 26	Any size	8,000	1.8370% 13.1576% 3.7030%
PR	1/11- 1/26 high quarter wages	7	133	26	Any size	7,000	1.40% 5.40% 2.90%
RI	4.62% high quarter wages + greater of \$10 or 5% of the benefit rate per dependent up to 5 dependents	68- 118	546- 682	8-26	Any size	19,000	1.69% 9.79% 2.36%
SC	1/26 high quarter wages	20	326	13-26	20 weeks or 1,500 in any quarter	7,000	1.14% 6.00% 3.40%
SD	1/26 high quarter wages	28	309	15-26	20 weeks or 1,500 in any quarter	10,000	0 8.50% 1.20%
TN	1/26 of average 2 highest quarters	30	275	13-26	20 weeks or 1,500 in any quarter	9,000	0.50% 10.00% 2.70%
TX	1/25 high quarter wages	59	406	10-26	20 weeks or 1,500 in any quarter	9,000	0.26% 6.26% 2.70%
UT	1/26 high quarter wages	29	451	10-26	Any size	28,300	0.20% 9.20% 1.20%
VT	Wages in the 2 highest quarters divided by 45	64	425	26	20 weeks or 1,500 in any quarter	10,000	0.80% 6.50% 1.00%
VA	1/50 of the 2 highest quarters	54	378	12-26	20 weeks or \$1,500 in any quarter	8,000	0.18% 6.28% 2.50%
VI	1/26 high quarter wages	33	462	13-26	Any size	22,200	0 6.00% 1.00%

**Appendix III: Major Characteristics of State  
UI Programs, as of March 2010**

<b>State</b>	<b>Weekly benefit formula</b>	<b>Minimum weekly benefit</b>	<b>Maximum weekly benefit</b>	<b>Number of benefit weeks</b>	<b>Minimum payroll size for benefit eligibility</b>	<b>2010 taxable wage base (per worker) (italics = indexed to wages)</b>	<b>2010 minimum &amp; maximum employer tax rates New employer rate</b>
WA	3.85% of average of high 2 quarters in base period	\$133	\$560	1-26	Any size	<i>36,800</i>	0 5.40% Industry average%
WV	1% annual wages	24	424	26	20 weeks or 1,500 in any quarter	12,000	1.50% 7.50% 2.70%
WI	4% high quarter wages up to maximum weekly benefit amount	54	363	14-26	20 weeks or 1,500 in any quarter	12,000	0 8.50% 3.25%
WY	4% high quarter wages	31	438	11-26	Any size	<i>22,800</i>	0.30% 9.10% 1.60%

Source: ETA, "Significant Provisions of State UI Laws," revised March 2010.

\*For those states with "any size," all workers are covered regardless of payroll size or weeks worked. States may have different thresholds for agricultural, domestic, and nonprofit employing units.

# Appendix IV: Various UI Program Statistics

**Table 7: States with Loans from the Federal Unemployment Account, as of December 31, 2009, and April 1, 2010**

(Dollars in Millions)

State	12/31/09 balance	4/1/10 balance
Alabama	\$146.1	\$269.0
Arizona		22.5
Arkansas	222.6	318.2
California	5,984.7	8,456.5
Colorado		188.1
Connecticut	179.6	423.9
Delaware		2.6
Florida	951.7	1,496.5
Georgia	70.0	337.0
Idaho	107.1	187.3
Illinois	1,168.5	2,081.1
Indiana	1,488.6	1,807.7
Kansas		65.8
Kentucky	576.7	759.8
Maryland		103.9
Massachusetts		278.9
Michigan	3,159.1	3,797.1
Minnesota	281.1	641.9
Missouri	474.3	690.2
Nevada	127.1	331.9
New Hampshire		24.1
New Jersey	964.1	1,569.9
New York	2,160.2	3,032.0
North Carolina	1,606.7	2,138.7
Ohio	1,727.9	2,229.5
Pennsylvania	1,871.5	2,814.3
Rhode Island	127.5	204.2
South Carolina	692.0	852.0
South Dakota	7.7	22.8
Texas	1,322.5	2,035.0
Vermont		23.9
Virgin Islands	8.4	12.9
Virginia	122.4	318.3
Wisconsin	922.0	1,343.8
United States	\$26,470.2	\$38,881.4

Source: Employment and Training Administration, Department of Labor.



**Table 8: UI Contributions, Benefits, and Reserves as a Percentage of Total UI-Eligible Wages, 1979-2008**

<b>Year</b>	<b>Contributions</b>	<b>Benefits</b>	<b>Net reserves</b>
1979	1.28	0.91	0.91
1980	1.11	1.34	0.64
1981	1.03	1.17	0.51
1982	1.04	1.76	-0.23
1983	1.18	1.44	-0.47
1984	1.37	0.92	0.16
1985	1.31	0.96	0.68
1986	1.16	0.99	0.99
1987	1.05	0.81	1.38
1988	0.97	0.69	1.71
1989	0.86	0.71	1.92
1990	0.75	0.86	1.88
1991	0.71	1.20	1.49
1992	0.78	1.10	1.19
1993	0.88	0.92	1.25
1994	0.92	0.86	1.32
1995	0.87	0.80	1.40
1996	0.80	0.76	1.43
1997	0.73	0.64	1.50
1998	0.62	0.58	1.51
1999	0.56	0.56	1.47
2000	0.54	0.52	1.46
2001	0.52	0.81	1.24
2002	0.53	1.08	0.96
2003	0.67	1.03	0.64
2004	0.78	0.81	0.59
2005	0.82	0.69	0.67
2006	0.76	0.62	0.78
2007	0.67	0.64	0.80
2008	0.62	0.85	0.60
<b>Annual average, 1979-2008</b>	<b>0.86</b>	<b>0.90</b>	<b>1.04</b>

Source: Unemployment Insurance Financial Data Handbook, Employment and Training Administration, Dept. of Labor.

**Table 9: UI-taxable Wages as a Percentage of Total UI-eligible Wages, States with Indexed Taxable Wage Base vs. Other States, 1979-2008**

<b>Year</b>	<b>U.S. overall</b>	<b>States with indexed base</b>	<b>Non-indexing states</b>
1979	0.47	0.59	0.50
1980	0.45	0.57	0.47
1981	0.42	0.57	0.44
1982	0.41	0.57	0.43
1983	0.43	0.58	0.46
1984	0.43	0.58	0.45
1985	0.42	0.58	0.44
1986	0.41	0.57	0.43
1987	0.40	0.57	0.41
1988	0.39	0.55	0.40
1989	0.39	0.56	0.40
1990	0.38	0.56	0.38
1991	0.37	0.54	0.37
1992	0.36	0.56	0.36
1993	0.36	0.56	0.36
1994	0.36	0.57	0.36
1995	0.35	0.57	0.35
1996	0.34	0.56	0.34
1997	0.33	0.56	0.33
1998	0.32	0.55	0.32
1999	0.32	0.55	0.31
2000	0.31	0.55	0.31
2001	0.30	0.55	0.30
2002	0.30	0.56	0.29
2003	0.29	0.56	0.29
2004	0.29	0.55	0.27
2005	0.29	0.55	0.27
2006	0.28	0.55	0.26
2007	0.27	0.54	0.25
2008	0.27	0.53	0.25
<b>Change, 1979-2008</b>	<b>-0.20</b>	<b>-0.06</b>	<b>-0.25</b>

Source: GAO calculations based on data from Unemployment Insurance Financial Data Handbook, Employment and Training Administration, Department of Labor.

**Table 10: States with UI Solvency or Social Cost Taxes as of 2010**

<b>State</b>	<b>Purpose of tax</b>	<b>State</b>	<b>Purpose of tax</b>
AL	Social cost	NY	Solvency
AK	Solvency	OH	Social cost
AR	Solvency	OK	Solvency
CO	Solvency & social cost	PA	Solvency & social cost
DE	Solvency	RI	Solvency
IL	Solvency	TX	Solvency & social cost
LA	Solvency & social cost	UT	Social Cost
MA	Solvency	VA	Solvency & social cost
MN	Solvency	WA	Solvency & social cost
NH	Solvency	WI	Solvency
NJ	Solvency	WY	Social Cost

Source: ETA, Comparison of State Unemployment Insurance Laws, January 1, 2010.

# Appendix V: Comments from the Department of Labor

U.S. Department of Labor

Assistant Secretary for  
Employment and Training  
Washington, D.C. 20210



**APR - 2 2010**

Mr. Andrew Sherrill  
Director  
Education, Workforce, and Income Security Issues  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, D.C. 20548

Dear Mr. Sherrill:

The Employment and Training Administration (ETA) is in receipt of the draft Government Accountability Office (GAO) report entitled, "Unemployment Insurance Trust Funds: Long-Standing State Financing Policies Have Increased Risk of Insolvency" (GAO-10-440).

The report is both important and timely considering the serious crisis facing the financing of state Unemployment Insurance (UI) benefits, which is putting at risk the ability of the UI system to act as an effective stabilizer for the economy and may result in many states reducing their UI benefit levels. The report also accurately focuses on the role of state tax cuts as a leading cause in this crisis. However, the report does not explore the complex relationships between solvency, tax effort and differences in benefit adequacy. These are crucial issues which need to be addressed.

Given the enormity of the predicted level of borrowing during the current recession and the prolonged impact it will have on solvency and program viability moving forward, it was very fitting that GAO is pointing out the value of forward-funding for the program. GAO's policy options to improve long-term trust fund financing are welcomed by ETA, and we look forward to working with Congress and the states on strategies that will move state UI trust funds towards solvency, and to creating a system that will be more equitable among the states.

It is important to note, however, that there may be additional options to address solvency concerns, including options for greater Federal cost-sharing, such as full Federal payment of extended benefits and various re-insurance models. We would also like to point out that the option of having state tax rate adjustments occur more frequently than on an annual basis may be inconsistent with the purported goal of improving long-term trust fund financing. To enhance the forward-funding operation of state tax systems, it is the level of rates that is important rather than the speed of correction. The purpose of lagging tax rate changes is to forestall any tax rate increases until a recession has passed. The lack of forward-funding in this case has produced the result that states are now faced with raising employer taxes while the recession continues, a circumstance that would have

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**Appendix V: Comments from the Department  
of Labor**

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been avoided in great measure if there had been adequate forward-funding measures implemented.

Enclosed are ETA's technical comments on the draft report. If you would like additional information, please do not hesitate to call me at (202) 693-2700.

Sincerely,



Jane Oates  
Assistant Secretary

Enclosures

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# Appendix VI: GAO Contact and Staff Acknowledgments

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## Contact

Andrew Sherrill (202) 512-7215 or [sherrilla@gao.gov](mailto:sherrilla@gao.gov)

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## Staff

## Acknowledgments

In addition to the contacts above, Michael J. Collins, Mark M. Glickman, Kristy Kennedy, Charles A. Jeszeck, Jessica A. Botsford, Susan C. Bernstein, and James Bennett made important contributions to this report.

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# Related GAO Products

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*Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention.* [GAO-09-717](#). Washington, D.C.: August 10, 2009.

*Unemployment Insurance: More Guidance and Evaluation of Worker-Profiling Initiative Could Help Improve State Efforts.* [GAO-07-680](#). Washington, D.C.: June 14, 2007.

*Human Service Programs: Demonstration Projects Could Identify Ways to Simplify Policies and Facilitate Technology Enhancements to Reduce Administrative Costs.* [GAO-06-942](#). Washington, D.C.: Sept. 19, 2006.

*Unemployment Insurance: States' Tax Financing Systems Allow Costs to Be Shared among Industries.* [GAO-06-769](#). Washington, D.C.: July 26, 2006.

*Unemployment Insurance: Enhancing Program Performance by Focusing on Improper Payments and Reemployment Services.* [GAO-06-696T](#). Washington, D.C.: May 4, 2006.

*Unemployment Insurance: Factors Associated with Benefit Receipt and Linkages with Reemployment Services for Claimants.* [GAO-06-484T](#). Washington, D.C.: March 15, 2006.

*Unemployment Insurance: Factors Associated with Benefit Receipt.* [GAO-06-341](#). Washington, D.C.: March 7, 2006.

*Unemployment Insurance: Better Data Needed to Assess Reemployment Services to Claimants.* [GAO-05-413](#). Washington, D.C.: June 24, 2005

*Unemployment Insurance: Survey of State Administrators and Contacts with Companies Promoting Tax Avoidance Practices.* [GAO-03-819T](#). Washington, D.C.: June 19, 2003.

*Unemployment Insurance: States' Use of the 2002 Reed Act Distribution.* [GAO-03-496](#). Washington, D.C.: March 6, 2003.

*Unemployment Insurance: Increased Focus on Program Integrity Could Reduce Billions in Overpayments.* [GAO-02-697](#). Washington, D.C.: July 12, 2002.

*Unemployment Insurance: Role as Safety Net for Low-Wage Workers Is Limited.* [GAO-01-181](#). Washington, D.C.: December 29, 2000.

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**Related GAO Products**

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*Unemployment Insurance: Program's Ability to Meet Objectives Jeopardized.* [GAO/HRD-93-107](#). Washington, D.C.: September 28, 1993.

*Unemployment Insurance: Trust Fund Reserves Inadequate to Meet Recession Needs.* [GAO/HRD-90-124](#). Washington, D.C.: May 31, 1990.

*Unemployment Insurance: Trust Fund Reserves Inadequate.* [GAO/HRD-88-55](#). Washington, D.C.: September 26, 1988.



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