TRANSMITTAL # 3

MEMORANDUM

November 5, 2009

TO: Workforce Development Council

FROM: Roger B. Madsen, Director

SUBJECT: Unemployment Insurance-Economic Impact

ACTION REQUESTED: None. Information Only

BACKGROUND:

The economy has had a dramatic impact on the Unemployment Insurance Trust Fund balances. Bob Fick, Communications Manager, prepared the attached document "Unemployment Insurance Trust Fund". This summarizes the impact on the fund and actions that the department has taken to maximize the fund balance while controlling the amount of tax increases that will be needed to restore the fund to pre-recession health.

I look forward to the opportunity to discuss this with the council at our November meeting.

Attachment

Contacts:	Primary:	Bob Fick	(208) 332-3570, ext. 3628
	Secondary:	John McAllister	(208) 332-3570, ext. 3101

Unemployment Insurance Trust Fund

The national recession drained Idaho's combined Unemployment Insurance Trust Fund in a matter of 19 months. The balance dropped from a high of $318 million in November 2007 to $43 million in June 2009.

The combined trust fund is currently broke even though one component has a positive balance. Because of the trust's two-part structure, the state began taking advantage of interest-free federal loans in June. The loans are being used as a money management tool.

Idaho's combined trust fund is comprised of the federal trust fund held in Washington, D.C., by the U.S. Department of Labor and the state-managed trust fund held in Idaho and invested by the state treasurer. Investment earnings on the federal trust are deposited into the trust to cover benefits. Investment earnings on the state-managed trust are deposited into the Special Administrative Fund, which can be used to pay benefits but also to offset reductions in federal operating grants. These investment earnings allowed the department to maintain its network of 25 local offices throughout the state despite multimillion-dollar cuts in federal operating grants in the years following the 2001 recession.

Idaho, Nebraska and North Carolina are the only three states with state-managed trusts.

Created in 1991, Idaho's state-managed trust has been financed by a 17 percent diversion of state unemployment insurance taxes during years when the balance in the state-managed trust is less than 1 percent of total taxable wages for the year and is less than half the balance of the federal trust. Both circumstances must occur, and that has happened six times since the state-managed trust was established. A seventh diversion was approved by the Legislature and governor in 2006 even though the state-managed trust balance was more than half the federal trust balance. Under current law future diversions are unlikely to occur.

Because the department can earn interest on the state-managed fund and take advantage of no-cost federal loans to continue paying benefits, the decision was made to maintain a balance in the state-managed trust and use the loans to weather the recession.

One month before the recession began in December 2007, Idaho had $118 million in the state-managed trust and $200 million in the federal trust. Idaho's 50,000 employers, beneficiaries of record low tax rates reflecting the economic expansion prior to 2008, paid only about $100 million in unemployment insurance taxes in 2008 while the recession pushed regular benefit payments to a record $210 million.

That dropped the balance in the federal trust to under $81 million at the end of 2008.

Job loss escalated dramatically in 2009 with weekly regular benefit payments peaking at over $11 million in February – double the previous weekly totals during 2008's record-setting demand. By early March, the federal trust was broke, and benefits were being paid with loans from the state-managed trust. That trust was drawn down from $118 million to just under $43 million by the end of May, and the department implemented its money management strategy using interest-free federal loans.

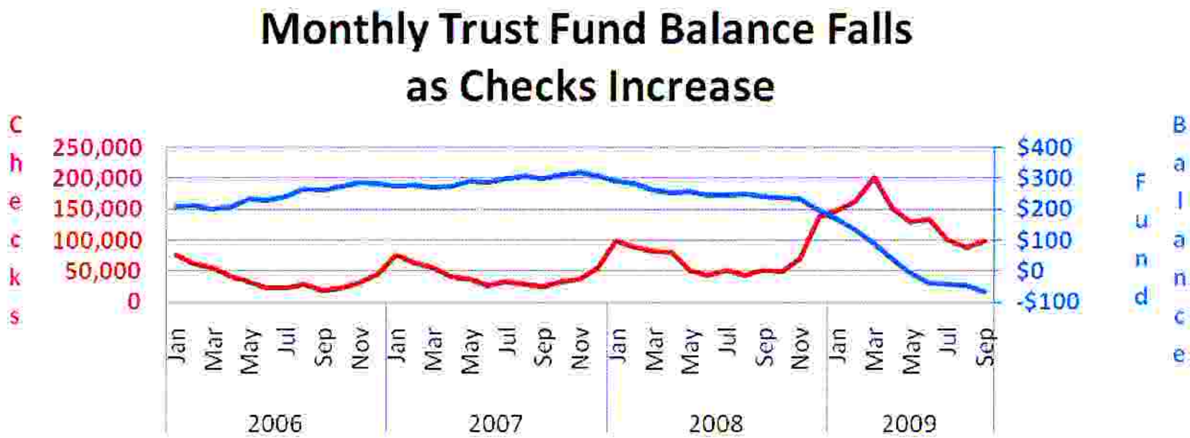
About $27 million was borrowed in June to continue benefit payments, and the balance in state-managed trust was rebuilt to just over $75 million with the deposit of $32.3 million the state received in incentive payments for securing legislative approve of modest benefit expansions. They extended benefits to laid-off part-time workers seeking new part-time jobs, laid-off workers enrolled in approved training and workers whose wage totals would meet minimum benefit requirements only if the most recent quarter of earnings was used in the calculation.

In July, the department borrowed another $25 million to continue benefit payments until the second quarter tax receipts were received at the end of that month. Receipts totaled $47 million, allowing the department to halt borrowing until late September, when those receipts were depleted. Since then, the department has borrowed over $20 million more. Borrowing will slow considerably for the next several weeks because third quarter employer tax receipts will be coming in. But that $30 million will be expended by mid-December or before, and another $25 million or so will be borrowed to finish out the year.

Since fourth quarter employer tax receipts due at the end of January are very low comparatively, the department expects to borrow another $80 million or more during the first four months of 2010 until employers make their first quarter tax payments at the end of April. At that point, the state will have borrowed about $193 million. More than half these loans will be repaid by the end of 2010 when the interest-free provision currently expires.

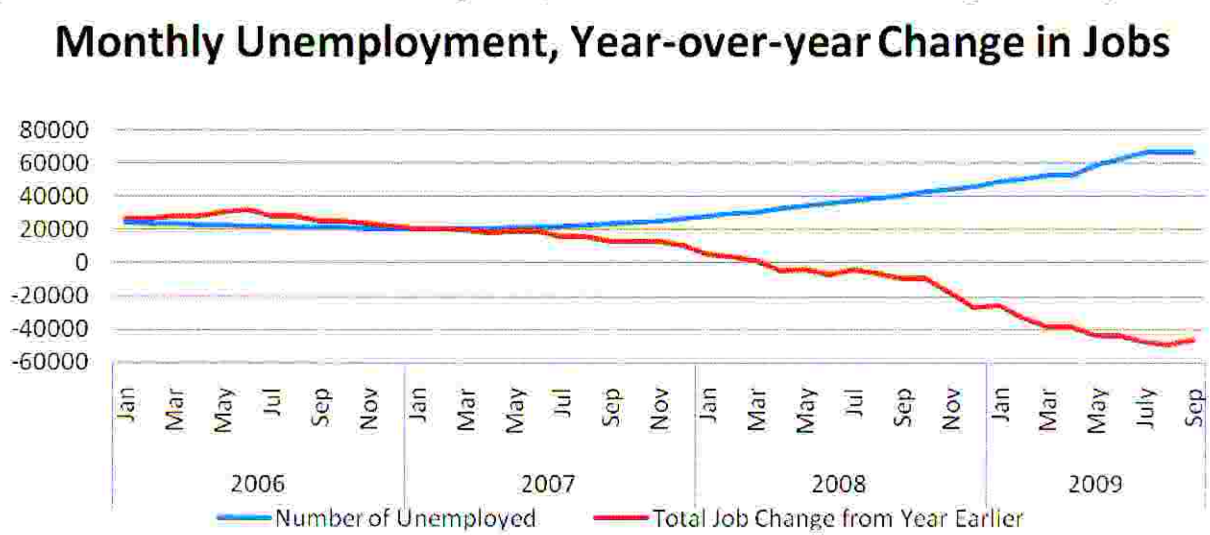
Twenty-one other states and the Virgin Islands have borrowed $20 billion to date. Seven have outstanding loan balances of over $1 billion with California $4.5 billion in the red, leading to speculation that the interest-free repayment period will be extended beyond 2010.

Idaho's weekly unemployment insurance benefit reports showed a steady decline in regular benefit payments until week 43, even into the fall when payments typically increase with seasonal layoffs. While this is favorable for the trust fund, it is not a solid indicator that the economy has turned around because about 1,000 people a week are exhausting their regular state benefits and moving onto extended benefits, which are financed completely by the federal government. The number of regular benefit claimants has dropped from a peak of 42,000 in late February to just under 19,000 in October, but the number of claimants on federal extended benefits has jumped from 7,200 in late February to nearly 18,000 in October. Currently about half the workers who claim regular state benefits exhaust those benefits before finding new jobs and move to federal extended benefits. This exhaustion rate is approaching the 54 percent rate at the worst of the 1980s recessions.



Idaho has already paid more than $340 million in regular state benefits, and jobless workers have received over $180 million more so far in federal extended and supplemental benefits. By year's end, regular state benefit payments will approach $400 million while federal extended and supplemental payments will total more than $200 million.

Even with the 70 percent increase in employer tax rates for 2009, revenue into the trust fund is projected at about $145 million – as much as $250 million short of the total payout in regular benefits. Since jobs peaked at 668,000 a few months before the recession began at the end of 2007, Idaho has lost 56,000 jobs. That two-year decline of 8.4 percent during this one recession is approaching the 9.5 percent job loss over the three years of the double-dip recessions in 1980-1982. The unemployment rate at 8.8 percent remains below the record high 9.4 percent from October 1982 through February 1983.



With the federal trust broke and an estimated $193 million in federal loans outstanding because benefit payments outstripped tax receipts despite the higher rate, tax rates for 2010 will likely double from the

2009 levels. The actual rates will not be determined until later this month. But they are expected to generate about $265 million in 2010 revenue, which should finance anticipated claims and repay about $120 million of the outstanding federal loans, reducing the loan balance below $70 million by the end of the year.

About $8 million will be borrowed in early 2011 to bridge the low fourth quarter 2010 tax payments to the much higher first quarter 2011 payments, and by fall 2011the federal loans should completely repaid.

This loan and repayment outlook is based on a recovering economy in 2010 and employer tax rates remaining at the anticipated 2010 level in 2011.

The dramatic employer tax rate increases are a product of the new rate and benefit formula agreed to by business and labor and approved by the Legislature in 2005. In addition to injecting equity and proportionality into the tax rate structure, one of the revision's most significant provisions cut the target balance for the trust fund in half – from $400 million to $200 million under 2005 economic circumstances.

Doing that made tax rates much more responsive to economic change – quickly pushing rates down during times of robust economic expansion and rapidly forcing rates higher when the economy contracts.

Making the revision at the beginning of one of the most robust expansions Idaho has experienced since the end of World War II provided Idaho employers with a significant financial benefit. In addition to the $200 million kept in employer hands in 2005 by halving the trust fund's target balance, the economic expansion in 2006 and 2007 drove tax rates down to a record low. That saved employers another $150 million they would have otherwise paid into the trust fund over those two years.

Because of those savings, Idaho employers met the recession in December 2007 with $350 million more in assets than they would have had under the old unemployment insurance financing structure.

With the rates responding rapidly to the downturn, which hit Idaho faster and harder than most other states, the rising tax rates in 2009 and 2010 will reclaim about $195 million of the savings the formula revision provided employers during the expansion.