

TRANSMITTAL #3

MEMORANDUM

DATE: November 22, 2005

TO: Workforce Development Council

FROM: Roger B. Madsen, Director

SUBJECT: Reed Act Appropriation

ACTION REQUESTED: Review and recommend approval of the proposed legislation

BACKGROUND:

This legislation would allocate to Idaho Commerce & Labor \$7 million from Idaho's Reed Act funds to partially offset cuts in federal support for unemployment insurance and employment services programs over the past decade. Although the bill simply gives the department access to the entire amount, the money would be withdrawn over two years to coincide with and partially compensate for further reductions in federal budget allocations.

SUPPORT HISTORY:

For the 2002-2003 budget year, the U.S. Department of Labor adopted a new allocation formula to distribute a declining pool of federal money to support state unemployment insurance programs. The old formula provided states a base amount for running the basic unemployment insurance program, then provided additional money as workload increased during deteriorating economic times. The new formula essentially operates on the theory that federal support for the unemployment insurance program is flat or declining. The formula allocates money among the states, taking cash from those with comparatively better economies and giving it to those with comparatively worse economies.

The effect of this change in Idaho's case was that the base grant amount in the post-recession years – when Idaho's economy was much stronger than most other states – was no longer sufficient to support basic unemployment insurance program services, especially as the Idaho economy got stronger relative to other states.

The unemployment insurance program is a critical part of Idaho's work force structure. During downturns, it provides limited financial support to laid-off workers, allowing them to pay for necessities and keep money moving through the local economy. But even in good times, it keeps qualified, skilled workers available for seasonal industries like logging, food processing, tourism and even some

construction trades where layoffs due to weather or the business cycle are a way of life. Without the interim financial support provided through the unemployment insurance program, these skilled workers would likely move to labor markets or other jobs that are not subject to any seasonal component.

In Idaho, the federal allocation went from over \$18 million for the 2002-2003 budget year to less than \$15 million for the current 2005-2006 budget year.

For employment services, which include the 24 local Commerce & Labor offices that link job seekers with employers needing qualified workers, the federal allocation to Idaho has dropped from over \$6.7 million to \$6.5 in recent years. This level could drop between 5 percent and 10 percent more depending upon the results of congressional negotiations on the current appropriations bill.

RISING COSTS:

The base grant amount from the federal government for unemployment insurance programs during the current year has dropped below the amount allocated to Idaho for the 1999-2000 budget year. In those six years, inflation has reduced the buying power of Idaho Commerce & Labor by 16.6 percent while pay raises legislated by the Idaho House and Senate and signed by the governor have increased the payroll 12 percent.

While federal increases in the base amount partially offset the impact of inflation and mandated pay raises through the 2002-2003 budget, the opposite has occurred since then.

To maintain the same level of basic unemployment insurance program services today that the state offered in 2002-2003 would require a budget of \$18.3 million. Idaho's allocation for 2005-2006 is \$14.4 million.

The financial situation is more significant for employment services programs since that federal allocation has essentially been unchanged for over a decade. But just since the 2002-2003 budget year, inflation and mandated pay raises on these programs means providing the same level of service today as four years ago would cost over \$8.1million. The federal allocation this year again is \$6.5 million.

The costs of the Iraq War and the hurricanes along the Gulf and Atlantic coasts assure additional reductions will be made in the annual federal allocations during at least the next several years, exacerbating the department's financial condition.

DEALING WITH REDUCTIONS:

Because Idaho Commerce & Labor has always operated on budget forecasts four years into the future, the agency has been aware of the federal funding trends and has had time to react to this point and absorb the cuts and expense increases without having to take drastic measures.

Technological advances, while expensive, have increased productivity without the need for more manpower. Staff reorganizations have occurred to refocus limited resources on priority programs and projects. In the past year, the agency has reduced staff in all its programs by 30 full-time equivalent

positions by lowering hours for part-time or temporary employees and consolidating work responsibilities in conjunction with employee attrition. As many as 30 more full-time equivalent positions will be eliminated in the coming year.

But the financial gap between actual federal support and the money it takes to pay for the basic services relied on by the 45,000 employers and 700,000 workers in Idaho has grown beyond the department's ability to avoid drastic service reductions. That gap today is \$5.5 million and expected to increase in the 2006-2007 and 2007-2008 budget years.

The \$3.5 million annual appropriation of Reed Act funds for the next two years would not completely bridge the financial gap. But without it, significant program cuts will be required. A major restructuring of unemployment insurance and employment services programs to close the funding gap would seriously affect the success the state has had over the past decade in making all services easily accessible to both employers and workers throughout the state.

THE SOLUTION:

Reed Act funds are generated by the Federal Unemployment Tax Act, which imposes a tax on employers of 0.8 percent on the first \$7,000 each employee earns every year. When the balance in that federal tax fund exceeds a pre-set amount, the excess is distributed to the states, which can only use the money for unemployment insurance benefits or, with approval of the Legislature, to run the unemployment insurance and employment services programs.

Idaho's last allocation of Reed Act funds was about \$32.5 million prior to 2002. In 2002, the Legislature approved \$7 million for computer upgrades, and this past session the Legislature approved \$900,000 for additional computer improvements, leaving a balance of \$24.4 million.

The proposed appropriation would reduce Idaho's Reed Act account to \$17.4 million by the end of the 2007-2008 budget year. This will have only a fractional impact on the unemployment insurance tax rates paid by employers – approximately two one-hundredths of 1 percent. The impact will also come during the 2008 tax year when the average unemployment insurance tax rate is expected under the current economic outlook to drop from 1 percent to an estimated 0.74 percent. Approval of the proposed appropriation will mean the tax rate will drop to 0.76 percent. The impact of the appropriation will lower the reduction in the average tax per employee from \$84 to \$78.

STAFF RECOMMENDATION:

The staff is requesting that the council endorse the appropriation of \$7 million from the Reed Act fund to maintain unemployment insurance and employment services programs throughout Idaho.

Contact: Primary Bob Fick (208) 332-3570, ext. 3628

Attachment Draft legislation.

AN ACT
APPROPRIATING SEVEN MILLION DOLLARS TO THE DEPARTMENT OF COMMERCE
AND LABOR OF THE STATE OF IDAHO PURSUANT TO SECTION 903 OF THE
FEDERAL SOCIAL SECURITY ACT, AS AMENDED, FOR EXPENSES INCURRED
FOR THE ADMINISTRATION OF THE UNEMPLOYMENT INSURANCE AND
EMPLOYMENT SERVICE PROGRAMS AND PROVIDING THAT SAID
APPROPRIATION IS AUTHORIZED BY AND SUBJECT TO THE LIMITATIONS
OF SECTION 72-1346(4), IDAHO CODE.

Be It Enacted by the Legislature of the State of Idaho:

SECTION 1. There is hereby appropriated out of the funds made available to the Department of Commerce and Labor of the State of Idaho, pursuant to Section 903 of the federal Social Security Act, as amended, the sum of \$7,000,000 for the payment of expenses incurred for the administration of the Unemployment Insurance and the Employment Service Programs. This appropriation is authorized by and subject to the limitations of Section 72-1346(4), Idaho Code.