

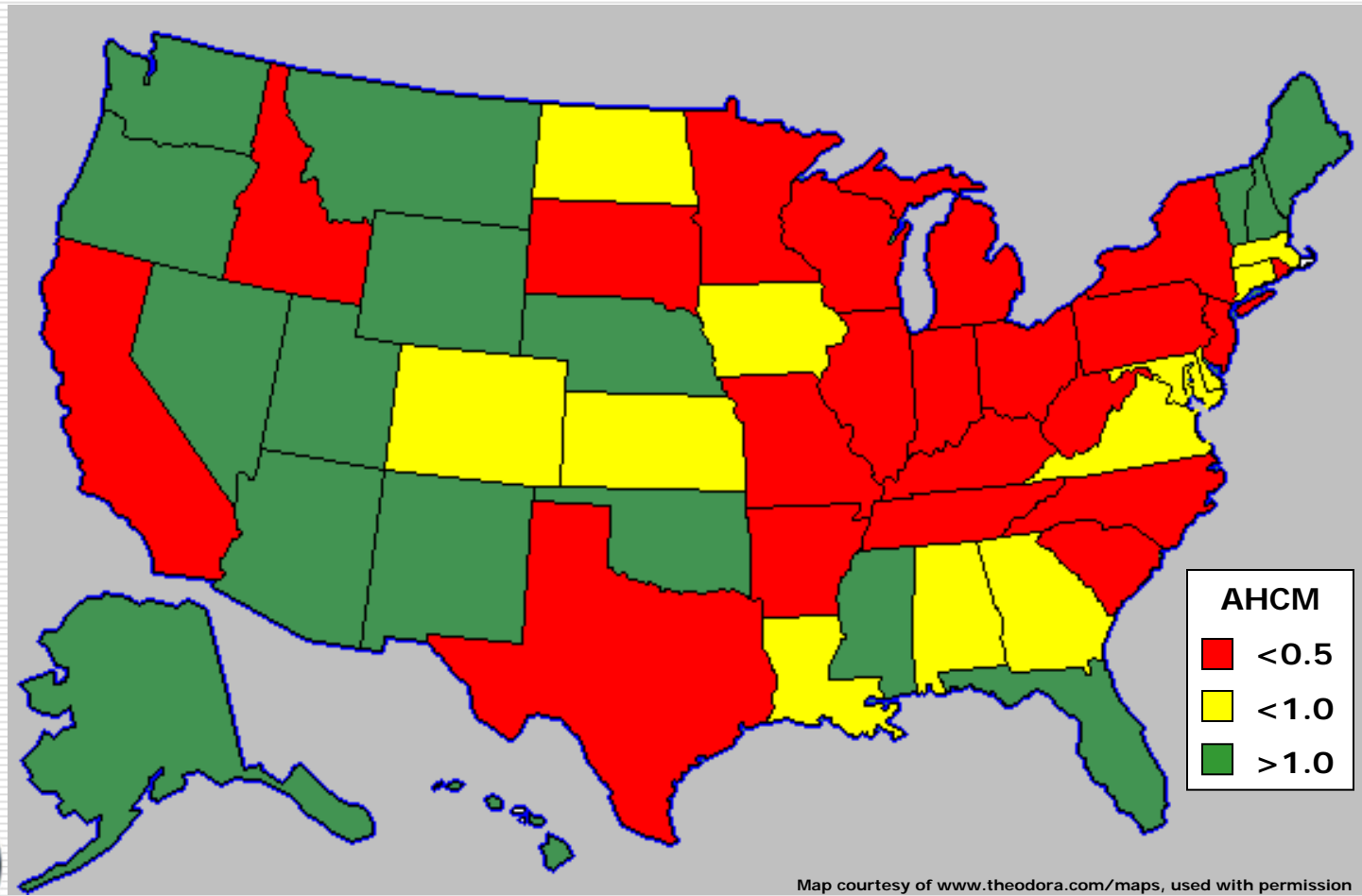
# Unemployment Insurance Financing

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Presentation to  
Employment Security Council  
October 4, 2011



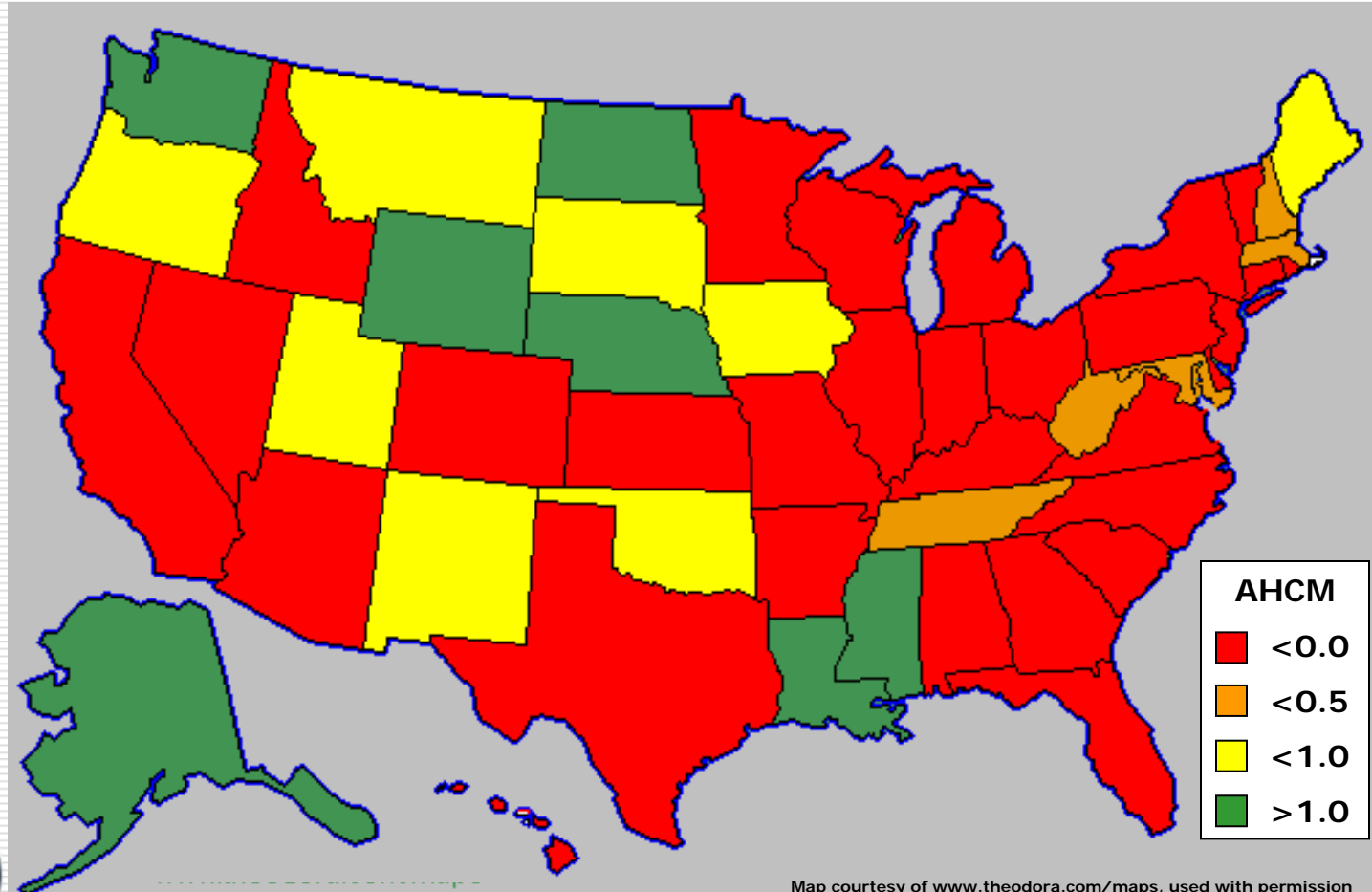
# National Perspective: National Solvency – 12/31/2007



Map courtesy of [www.theodora.com/maps](http://www.theodora.com/maps), used with permission



# National Perspective: National Solvency – 12/31/2010



AHCM	
	< 0.0
	< 0.5
	< 1.0
	> 1.0

Map courtesy of [www.theodora.com/maps](http://www.theodora.com/maps), used with permission



# National Perspective: Borrowing Across the Nation

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- ❑ At the beginning of the year, 30 states had loans outstanding in the form of either bonds or Title XII loans.
- ❑ As of September 27, 2011, 28 states and territories have \$38.0 billion in outstanding Title XII loans.
- ❑ 28 states owe interest on September 30 for Title XII loans.



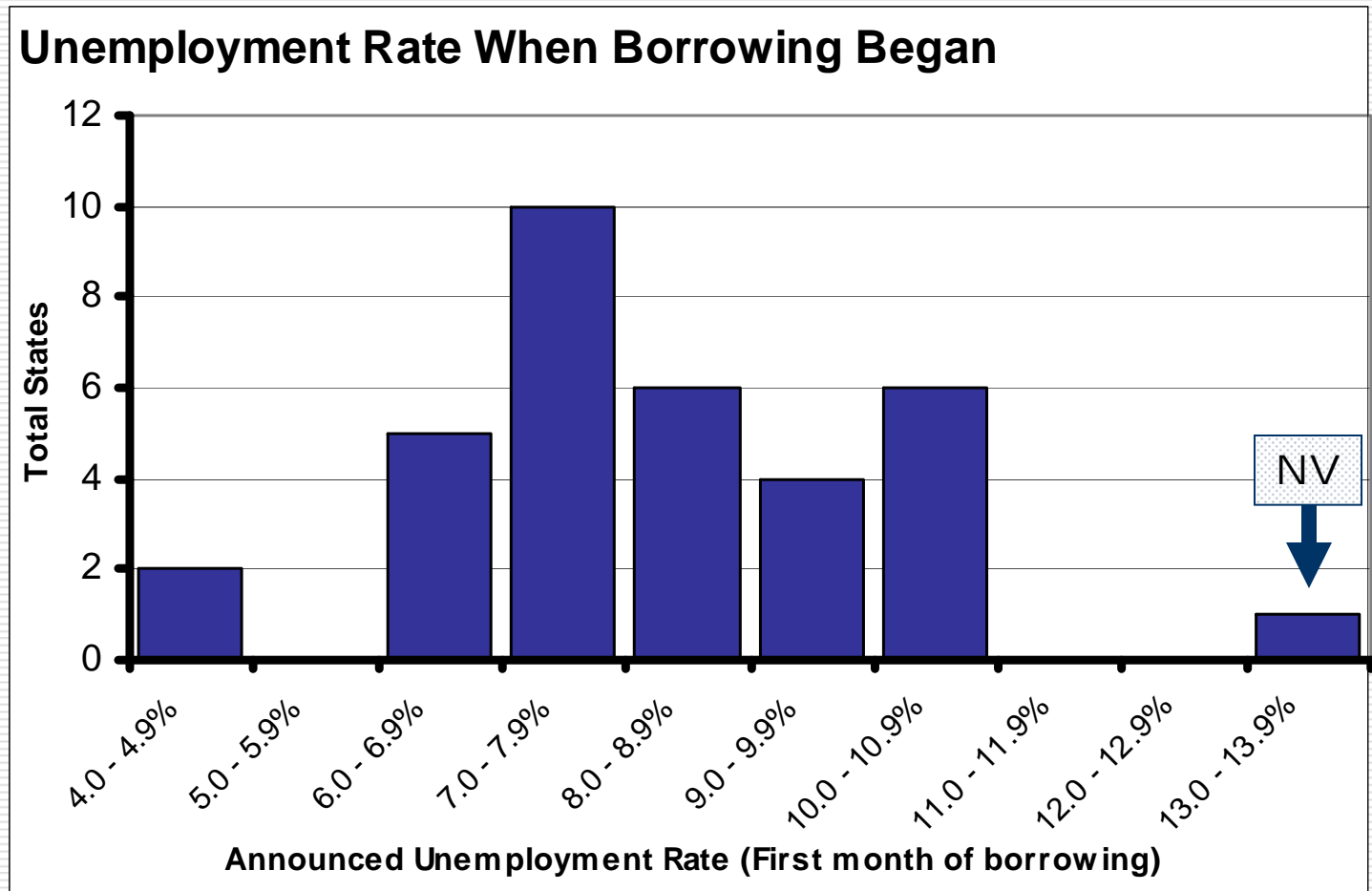
# Nevada's Trust Fund: Before the Recession

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- ❑ Nevada was reasonably prepared for the recession.
- ❑ In the quarter the recession began, Nevada had:
  - ❑ The 18<sup>th</sup> strongest Trust Fund
  - ❑ An Average High Cost multiple of 1.02 (Department of Labor recommends at least 1.0)
  - ❑ A state solvency multiple of 1.47 (calculated per NRS 612.550)

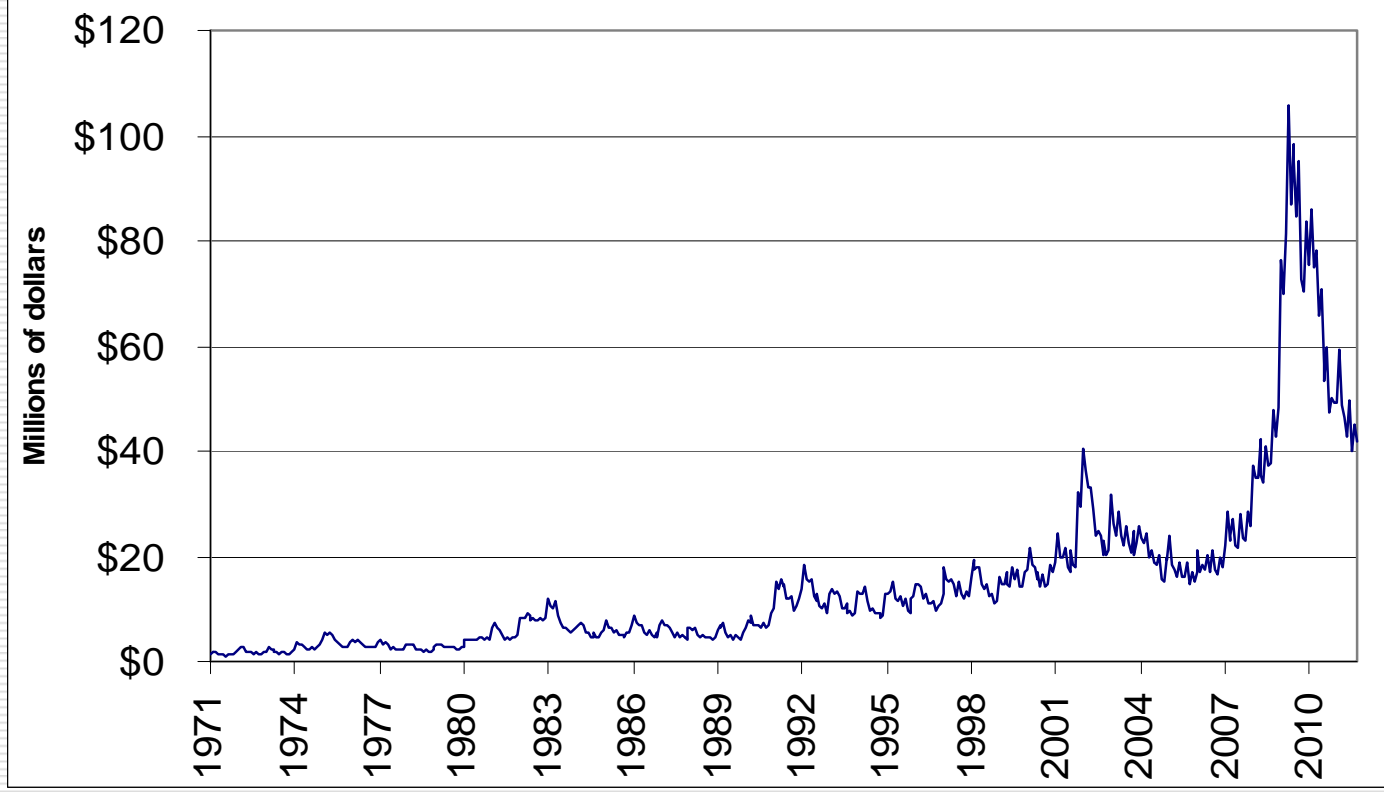


# Nevada's Trust Fund: What it Took to Borrow

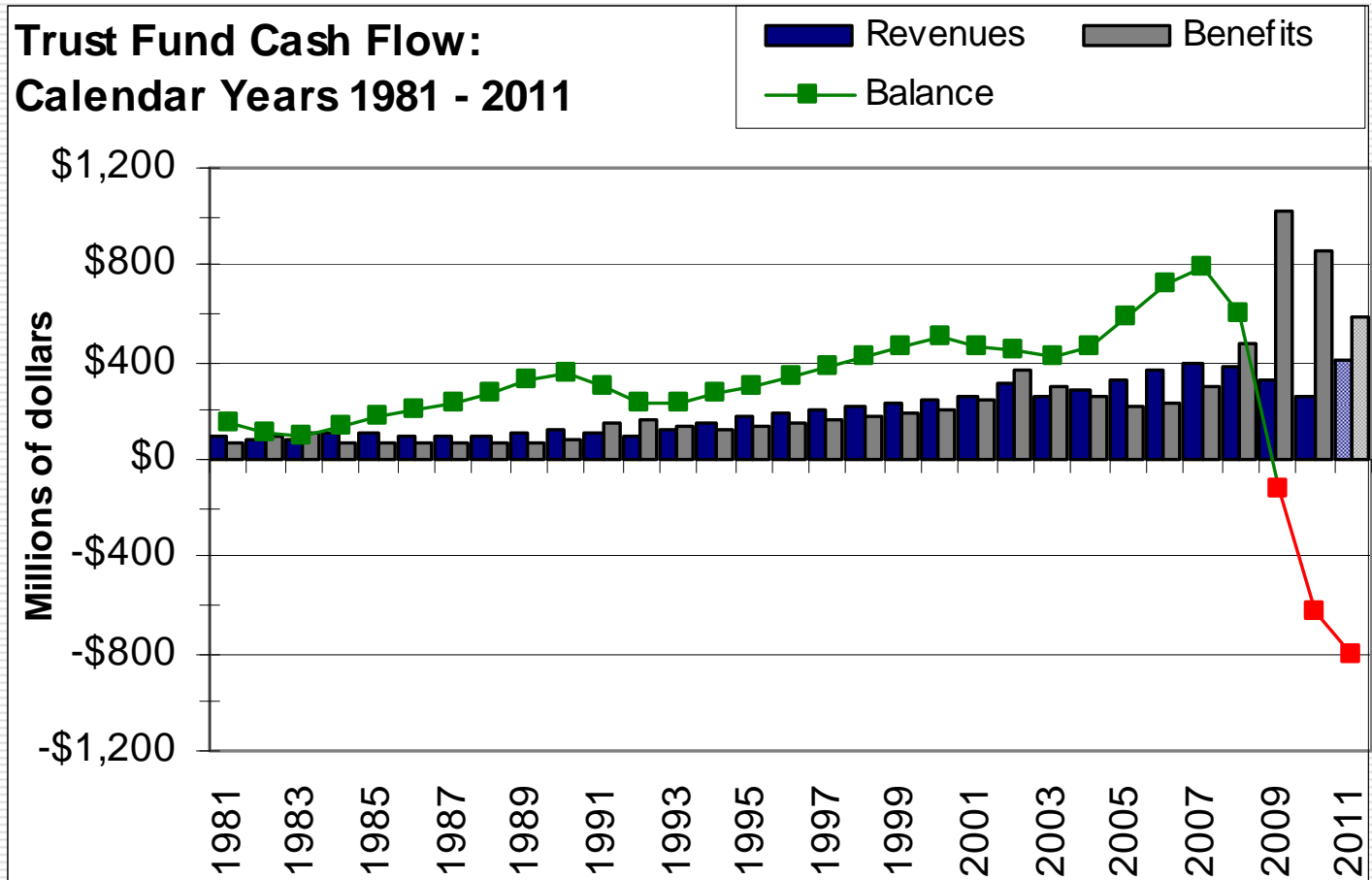


# Nevada's Trust Fund: Declining Benefit Payments

## Monthly Compensation: 1971 to Present

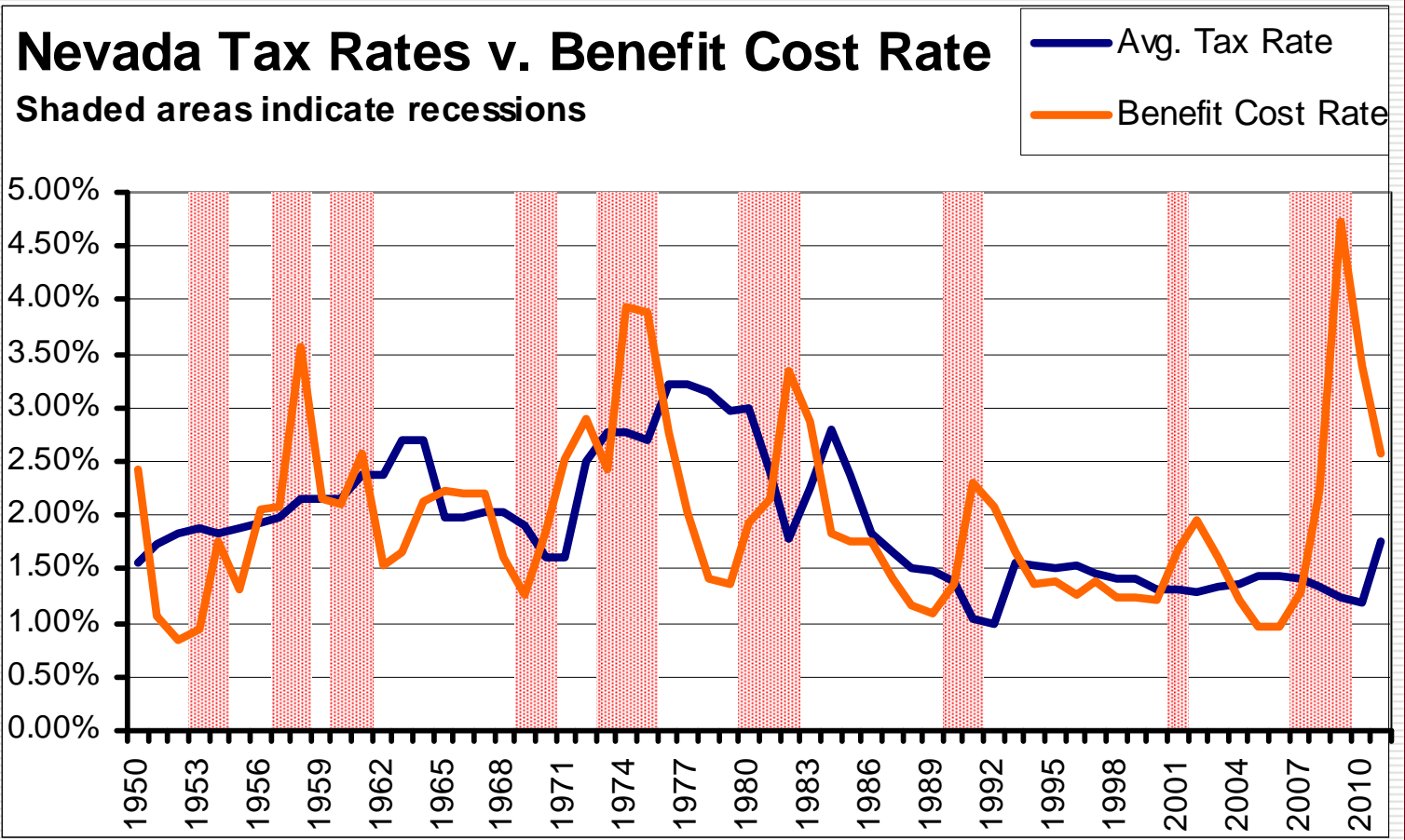


# Nevada's Trust Fund: Reduced Need for Borrowing





# Nevada's Trust Fund: Tax Rates and Benefit Costs



# Costs of Borrowing: FUTA vs. SUTA Taxes

## FUTA

- Fixed Wage Base: \$7,000
- Paid to Federal government
- Funds federal & state UI administration, Title XII loans
- Fixed tax rate: 6.2% minus 5.4% credit (0.8% overall)
- Rate dropped by 0.2% as of July 1, 2011 to 6.0% (0.6% after credit)

## SUTA

- Indexed Wage Base: \$26,400 in 2012
- Paid to Nevada
- Used only to pay benefits, or the principal of loans which were used to pay benefits.
- Average rate set each year by regulation, currently 2.00%



# Costs of Borrowing: FUTA Offset Credit Reduction

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- ❑ If a state uses Title XII to pay benefits, and has outstanding loans after 2 years, the Federal government begins reducing the FUTA credit.
- ❑ This increases the FUTA tax paid by employers.
- ❑ The longer a state is borrowing, the steeper the credit reduction becomes.
- ❑ All revenue generated by the increased portion of the FUTA tax is applied to the outstanding loan balance.



# Costs of Borrowing: Basic Credit Reduction

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- ❑ On the second January 1 with outstanding loans, the credit to employers is reduced by 0.3% (\$21 per employee).
- ❑ The credit is reduced by an additional 0.3% each subsequent year.
- ❑ In addition to the base reduction there is a potential additional reduction that begins in the fifth year of borrowing.
- ❑ The first 0.3% credit reduction will apply to Nevada for 2011 wages.



# Costs of Borrowing: Additional Credit Reduction

- ❑ On the fifth consecutive January 1 with outstanding loans, the “BCR Add-on” is applied.
- ❑ This Add-On takes the higher of 2.7% or the 5-year average Benefit Cost Ratio, and subtracts the state’s average tax rate.
- ❑ This reduction does not apply in any year if the state takes no action that would be expected to result in a net decrease in solvency, as determined by the U.S. Secretary of Labor, if the state applies by July 1.
- ❑ Example of BCR Calculation using a Benefit Cost Rate of 2.9%:
  - ❑ 2.9% - (2013 Average UI Tax Rate)
  - ❑ E.g. 2.9% - 2.0% = 0.9% (rounded)
  - ❑ The FUTA Credit may be reduced an additional 0.9%
- ❑ The size of the BCR Add-on is directly related to the average tax rate in the prior year.



# Costs of Borrowing: Illustrating FUTA Credit Reductions

Year	Basic Reduction	Basic CPE*	5-Year Benefit Cost Rate	Nevada SUTA Tax Rate	BCR Add On	Additional CPE*	Total CPE* Including Normal FUTA
2011	0.3%	\$21					\$63
2012	0.6%	\$42					\$84
2013	0.9%	\$63					\$105
2014	1.2%	\$84	2.9%	2.0%	0.9%	\$63	\$189
2015	1.5%	\$105	2.3%	2.0%	0.7%	\$49	\$196
2016	1.8%	\$126	2.0%	2.0%	0.7%	\$49	\$217
2017	2.1%	\$147	1.7%	2.0%	0.7%	\$49	\$238

\*Cost Per Employee

- ❑ Normal FUTA: 0.6% tax on first \$7,000 in wages, or \$42 per employee per year.
- ❑ Basic Reduction: 0.3% per year of borrowing.
- ❑ BCR Add-On: Nevada's SUTA Tax Rate subtracted from either 2.7% or the 5-year Benefit Cost Rate, whichever is larger. Begins in 5<sup>th</sup> year of borrowing. Waived if state takes no action resulting in net decrease in Trust Fund solvency.



# Costs of Borrowing: FUTA Offset Credit Caps

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- ❑ FUTA Offset Reductions can be capped if the state is making adequate progress toward restoring fund solvency
- ❑ The cap is the higher of:
  - ❑ A 0.6% credit reduction, or
  - ❑ The prior year's credit reduction



# Costs of Borrowing: FUTA Offset Credit Caps

- ❑ In order to cap the credit reduction, the state must meet four benchmarks:
  - ❑ No state action was taken from October 1 to September 30 which would result in a reduction of the state's unemployment tax effort.
  - ❑ No state action was taken from October 1 to September 30 which would result in a net decrease in solvency of the state UI system.
  - ❑ The state unemployment tax rate is greater than or equal to the 5-year average benefit cost rate for the 5 prior calendar years.
  - ❑ The state's outstanding loans from the Federal government are less than in the third prior year.





# Costs of Borrowing: Targeting Capped FUTA Rates

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- ❑ **Lowest Rate Possible (0.6%):**
  - ❑ Rate cannot be capped until 2013 (the first year the FUTA reduction would exceed 0.6%)
  - ❑ Average Tax Rate would need to be at least 3.0% in 2013
  - ❑ Loan balance on September 30, 2013 would need to be less than \$525.7 million.
- ❑ **Second-Lowest Rate Possible (0.9%):**
  - ❑ Average Tax Rate would need to be at least 2.9% in 2014
  - ❑ Loan Balance on September 30, 2014 would need to be less than \$742.2 million



# Costs of Borrowing: Why Cap FUTA Rates?

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- ❑ Relying on FUTA to repay borrowing takes many years to make a dent in borrowing, and does not restore solvency once borrowing is repaid.
- ❑ FUTA Taxes rely on the Federal \$7,000 wage base, putting an additional burden on employers of lower wage workers.
- ❑ Relying on state tax rates allows a more flexible, local review of steps to restore solvency.



# Costs of Borrowing: Interest Expenses

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- ❑ Interest on Title XII loans is due on September 30.
- ❑ Failure to pay this interest results in program decertification.
  - ❑ FUTA Rate immediately becomes 6.0%, increasing FUTA taxes by over \$400 million.
  - ❑ State loses access to Title XII Loans.
  - ❑ State loses all administrative UI Funding, worth about \$25 million per year.
- ❑ Funds were appropriated for 2011 and 2012 in AB 484 to cover interest costs in this biennium.



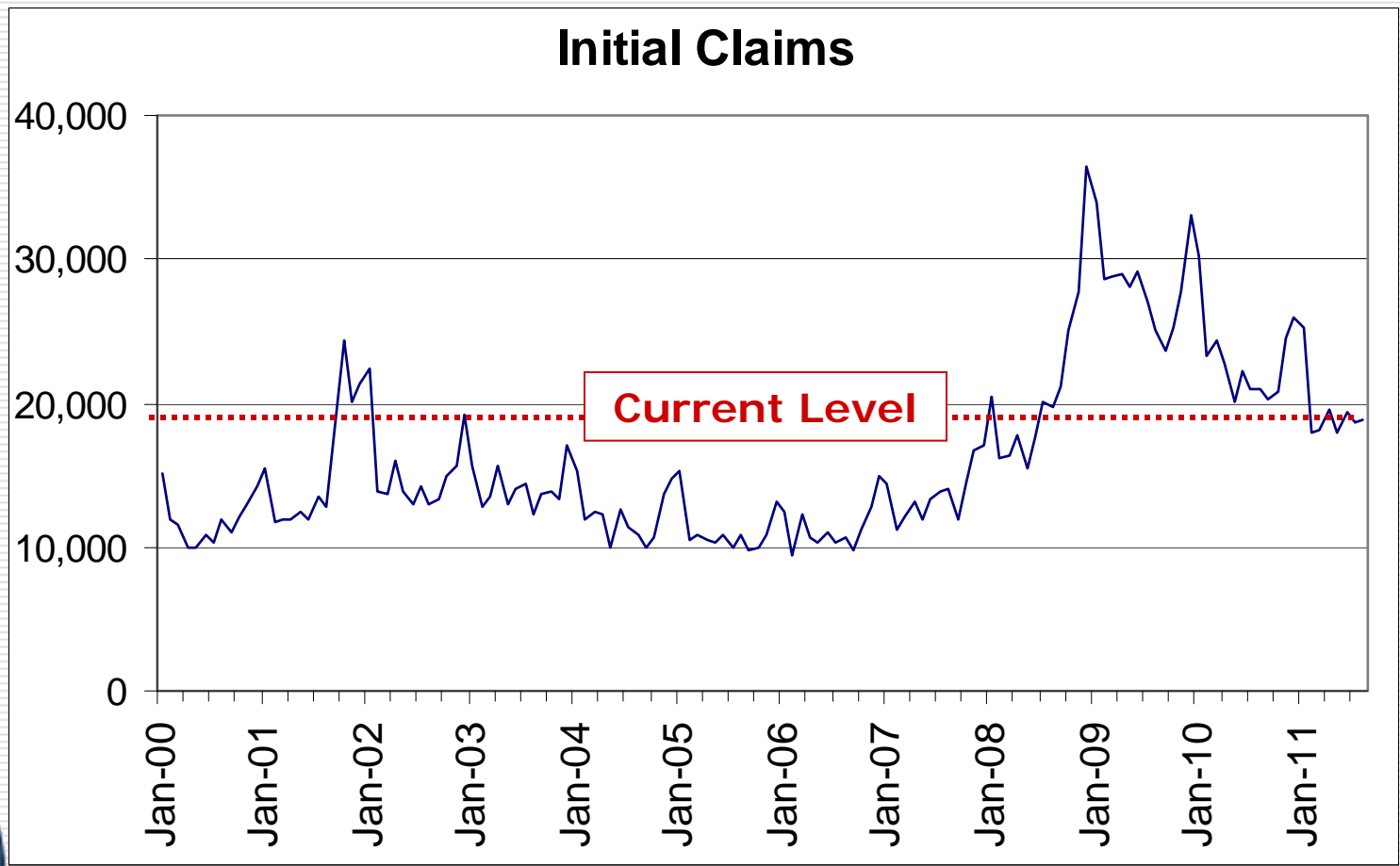
# Costs of Borrowing: Interest Charges for 2011

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- ❑ Interest accrual began on outstanding loans on January 1, 2011, reducing the interest expense this year.
- ❑ The interest rate charged is based on the interest earned on positive trust fund balances.
- ❑ The interest rate for 2011 is 4.08690135%
- ❑ Nevada's 2011 interest cost is \$22.6 million.
- ❑ Across all states, estimated 2011 interest charges are \$1.1 billion.

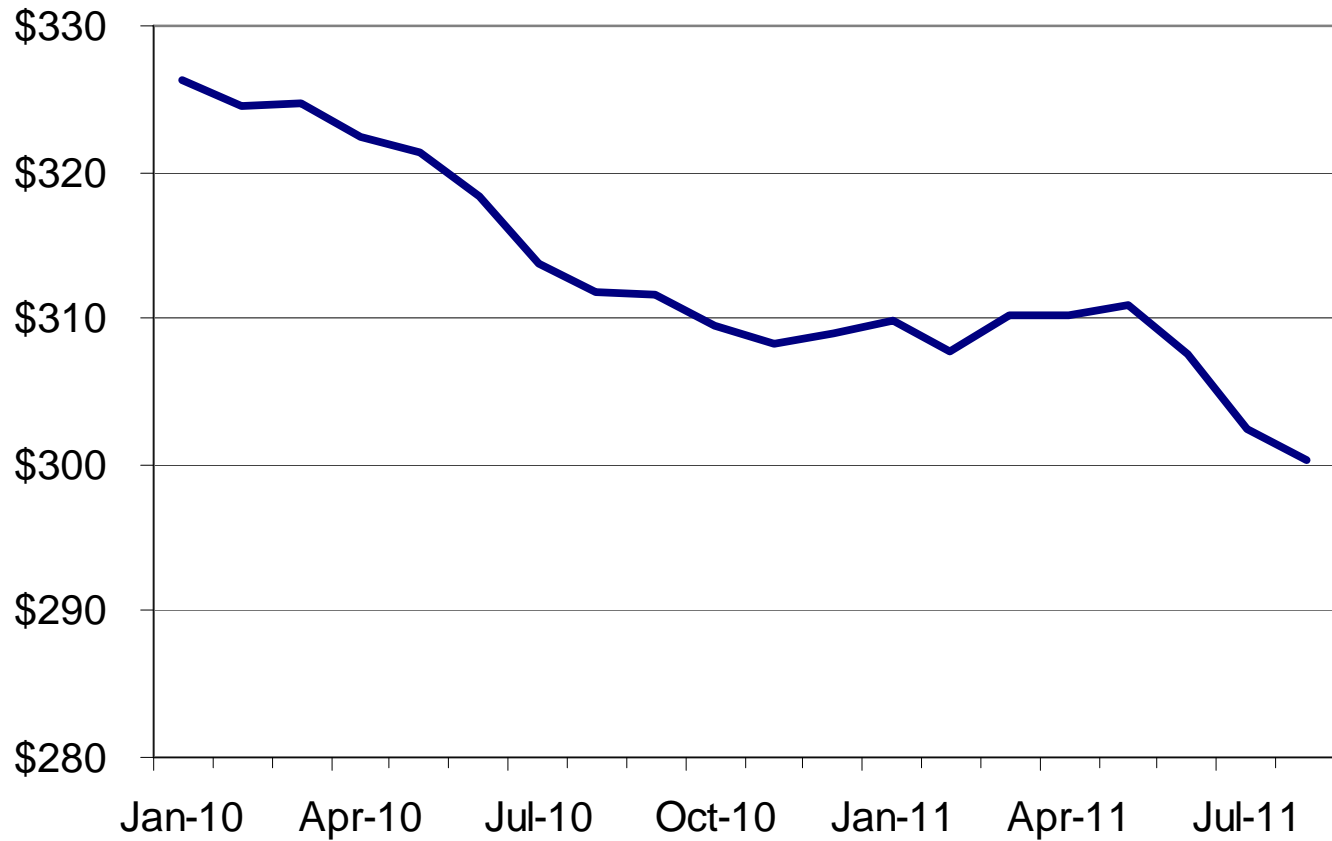


# 2011 Trends: Slowing Decline in Initial Claims

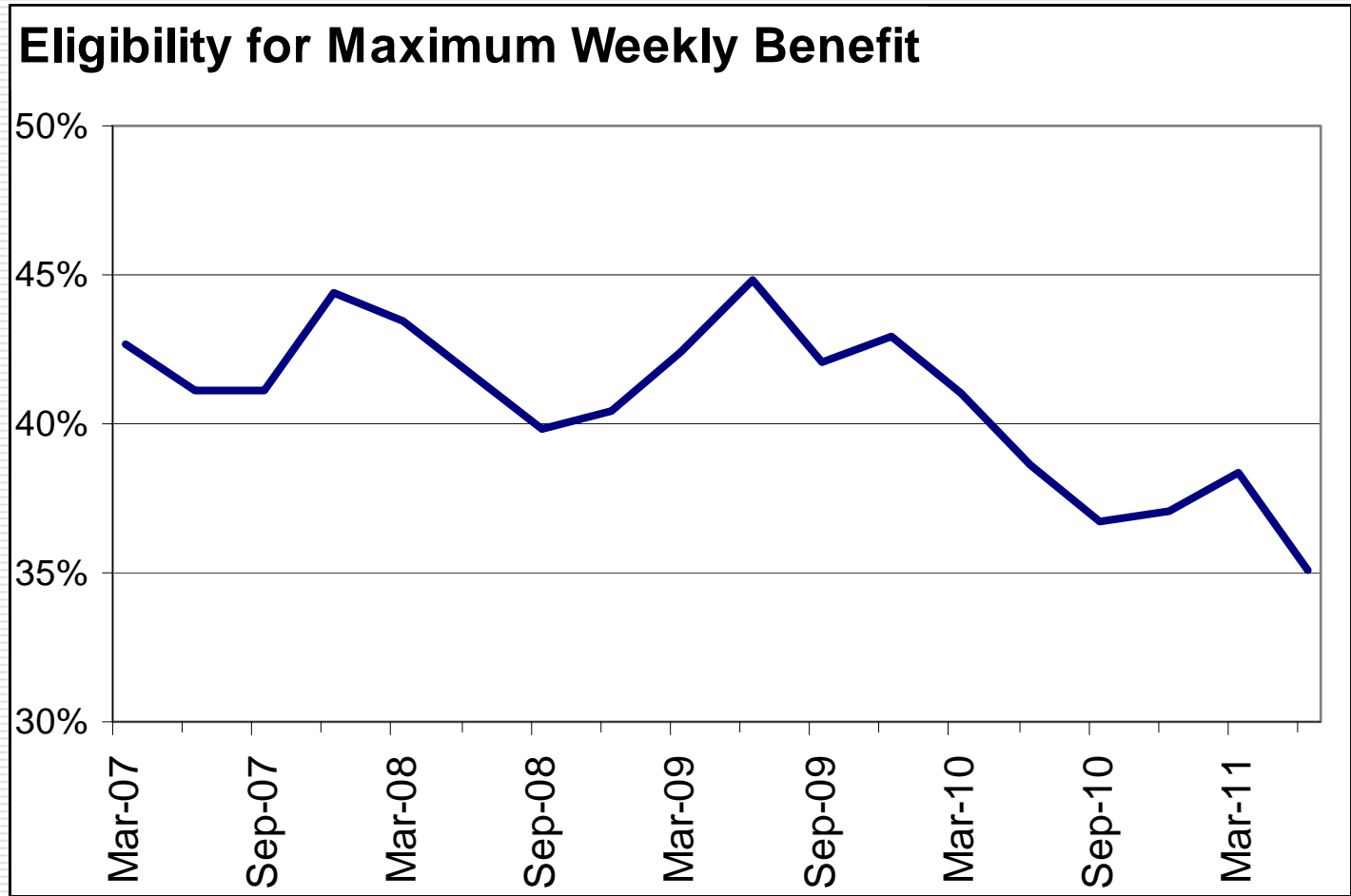


# 2011 Trends: Declining Weekly Benefits

**Average Weekly Benefit Payment: 2010-2011**

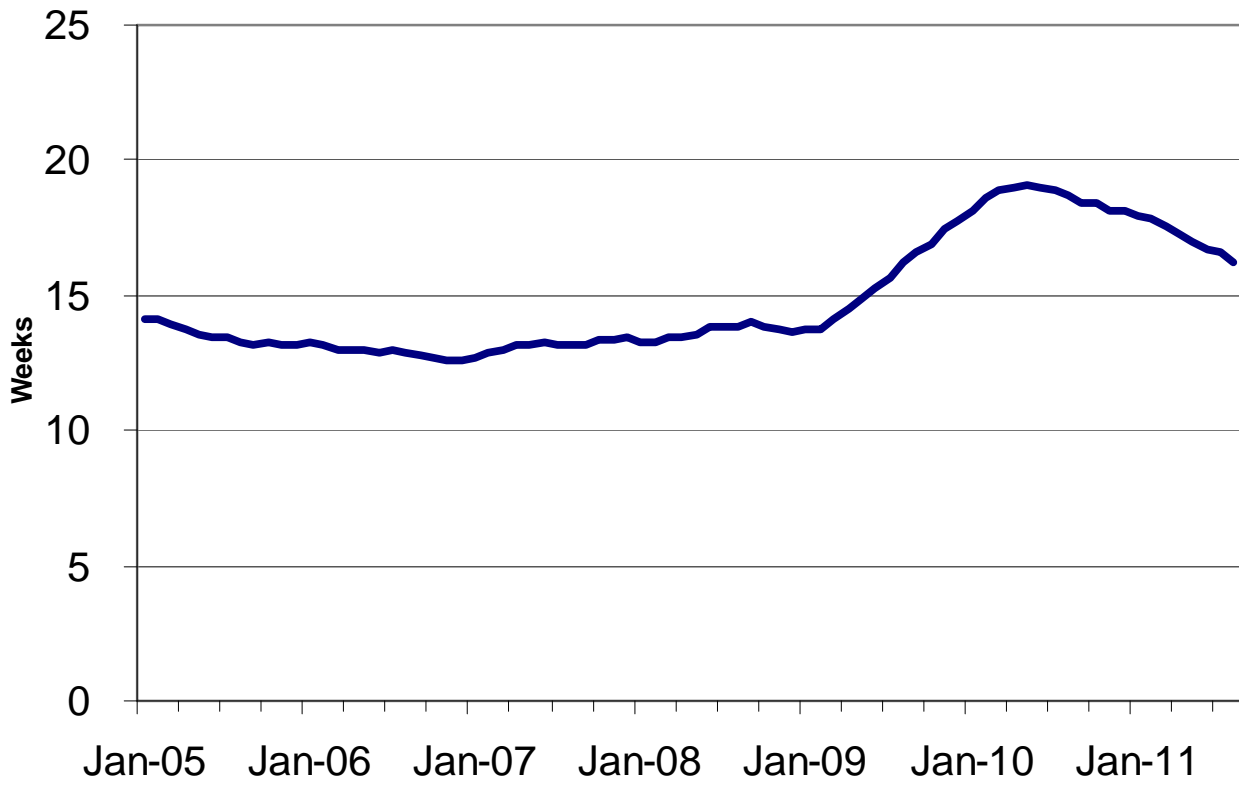


# 2011 Trends: Declining Benefit Eligibility



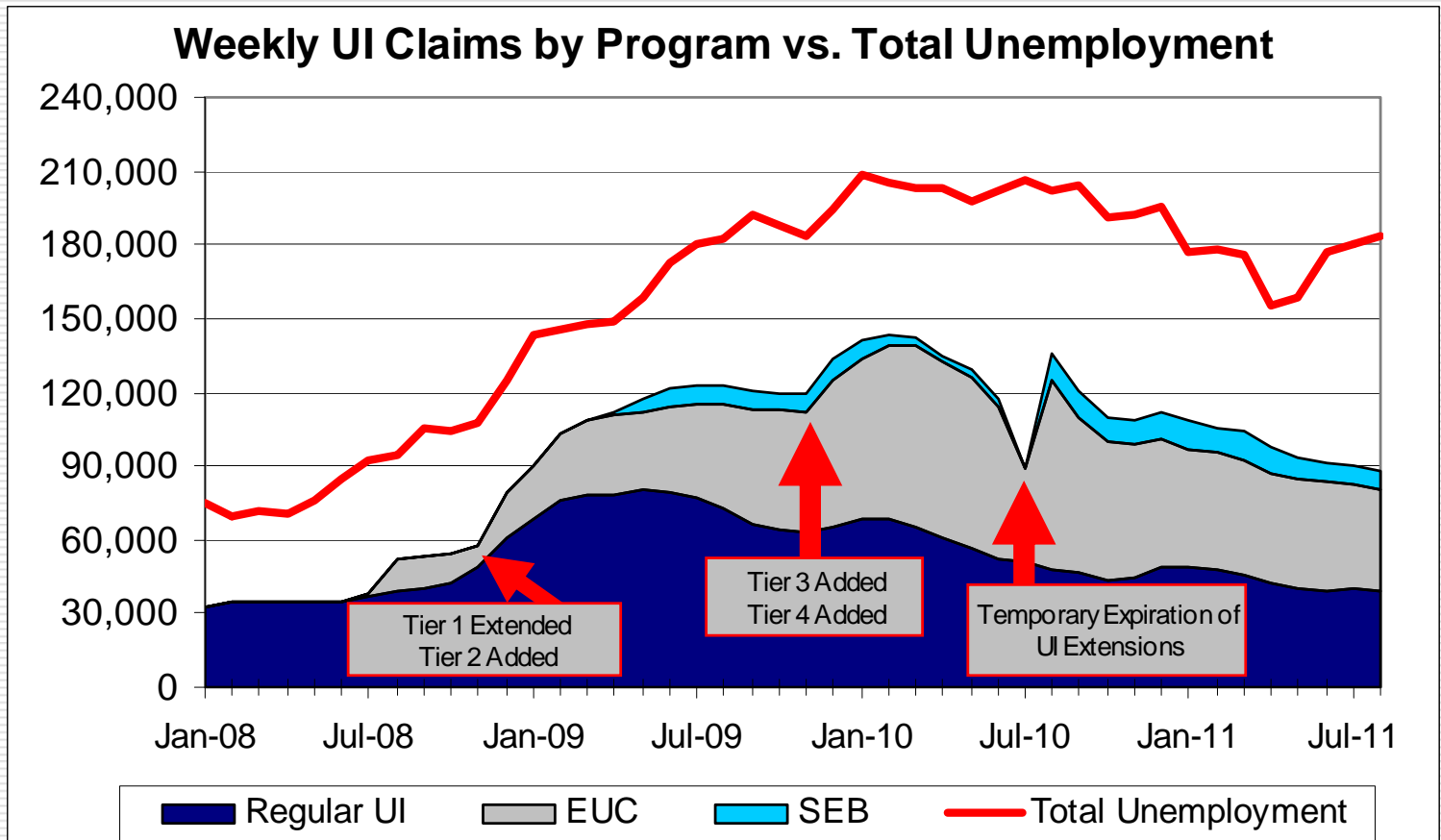
# 2011 Trends: Declining Benefit Use

**Average Duration of Regular Unemployment Benefits: 2005-2011**



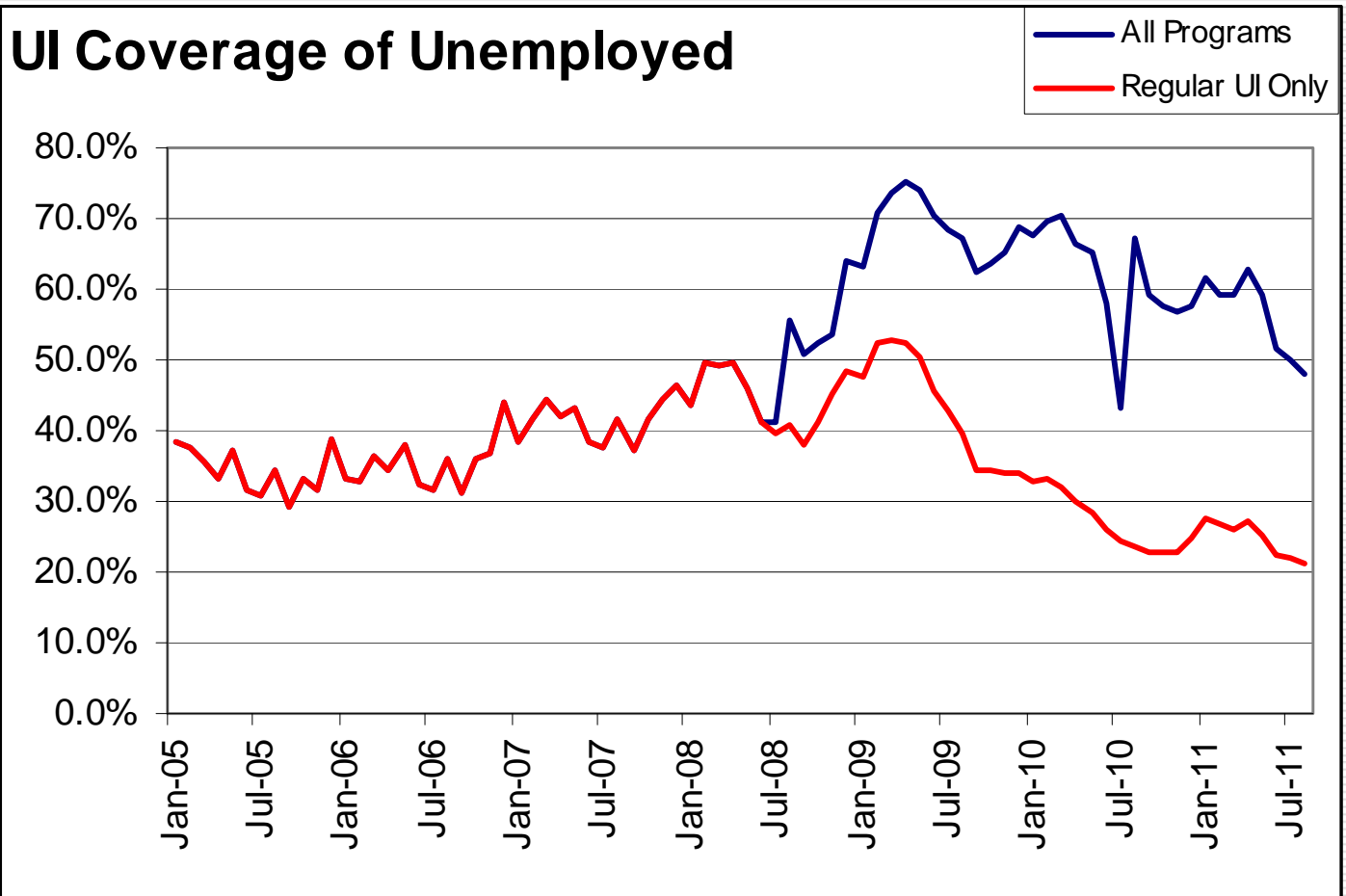


# 2011 Trends: Federally Paid Extensions

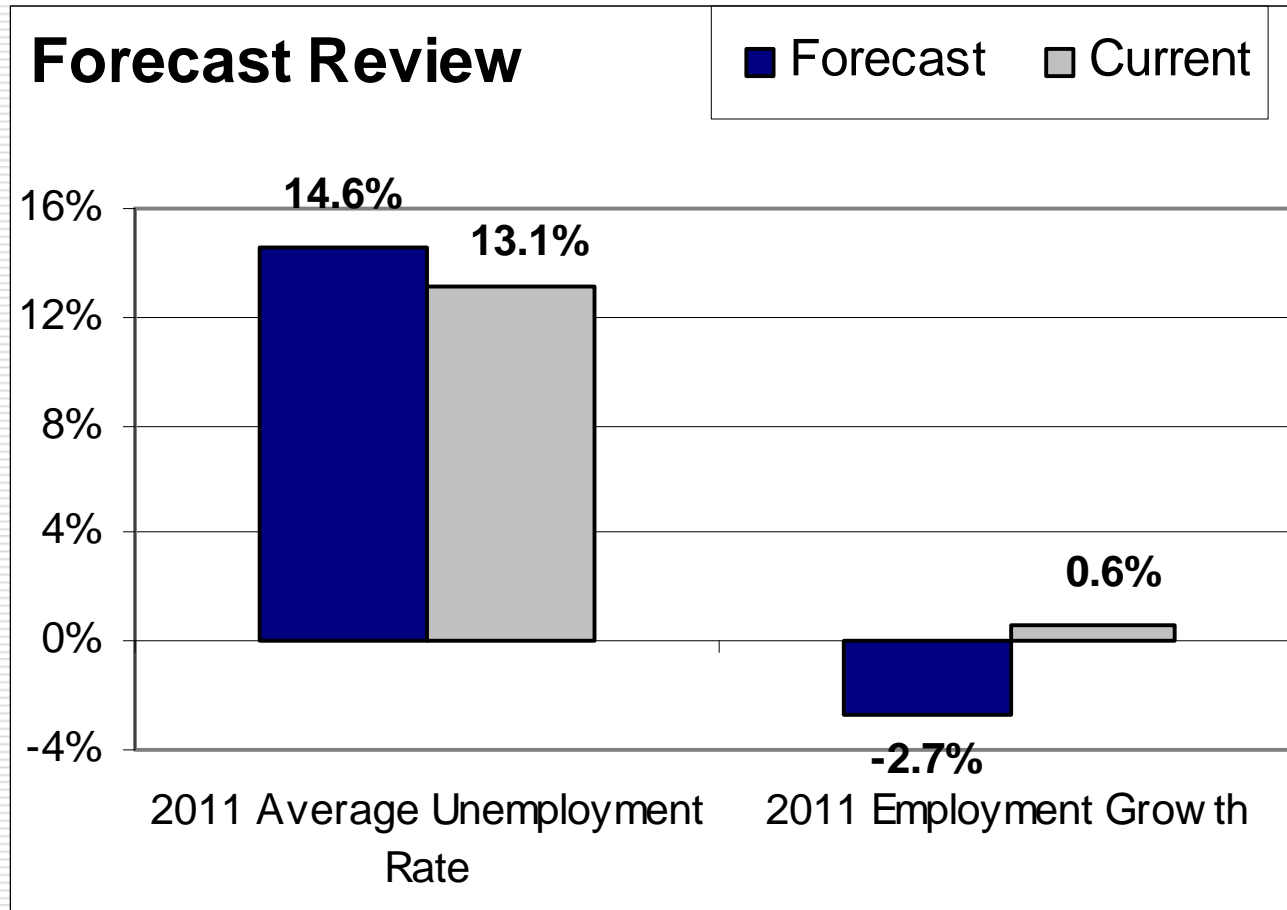


# 2011 Trends: Declining Support Levels

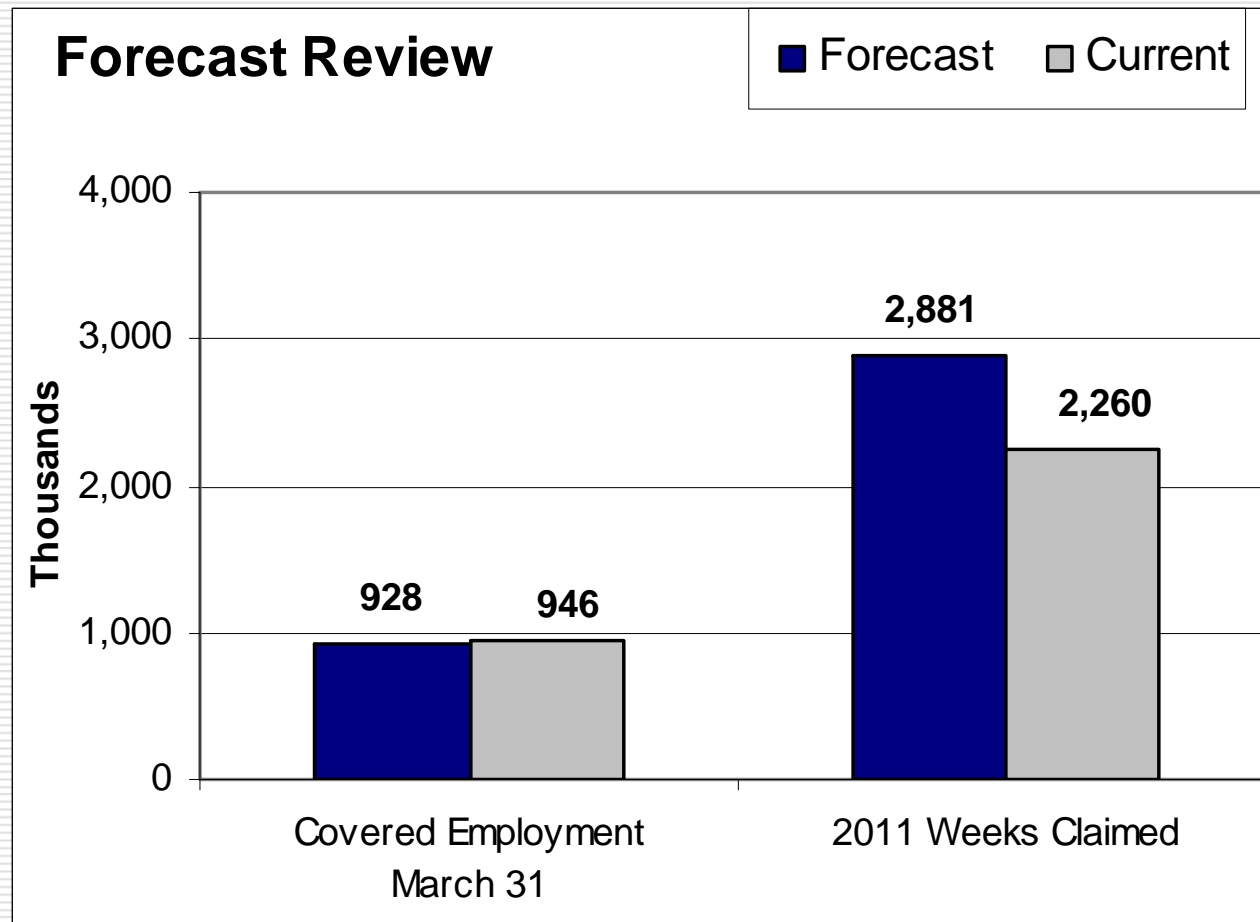
## UI Coverage of Unemployed



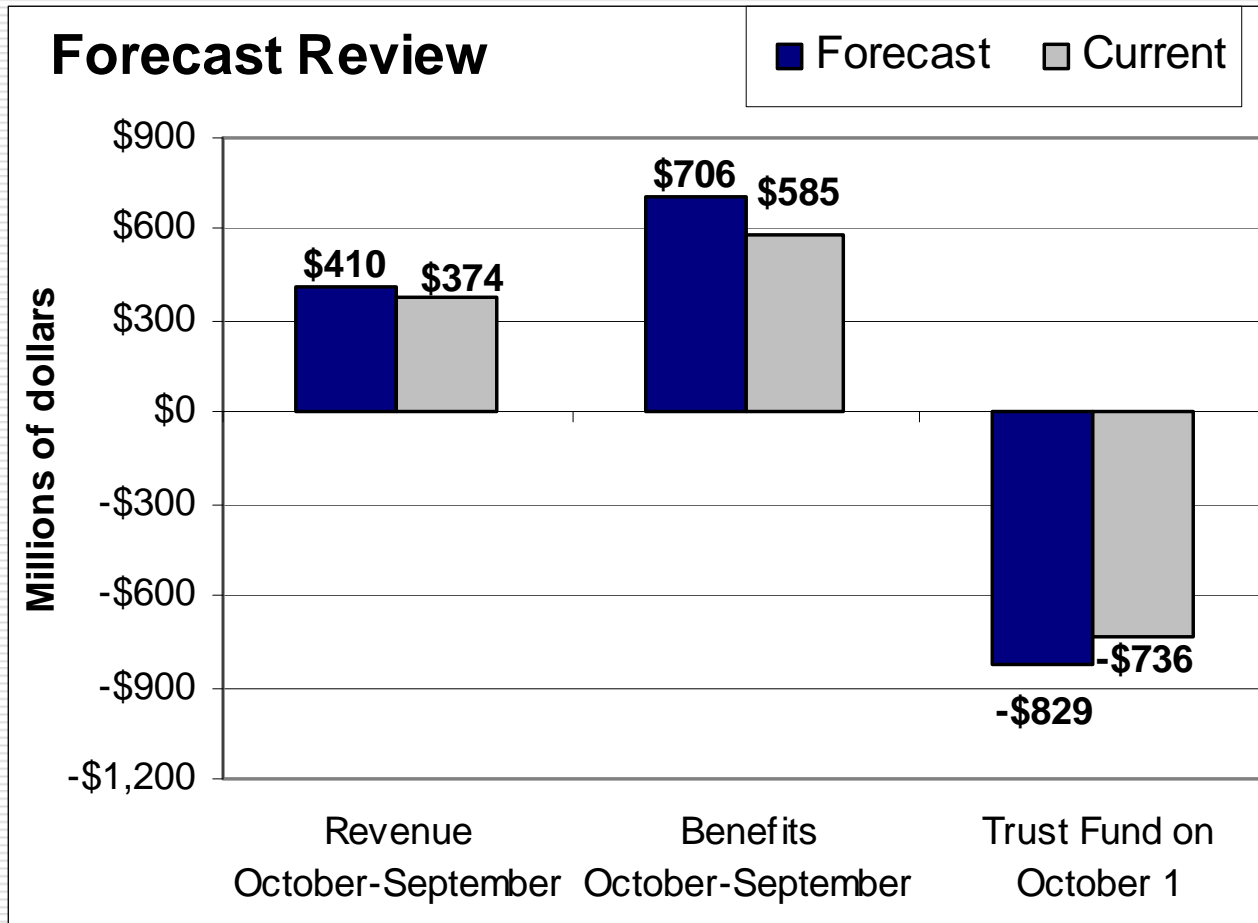
# 2012 Forecast: Review of Forecast for 2011



# 2012 Forecast: Review of Forecast for 2011



# 2012 Forecast: Review of Forecast for 2011



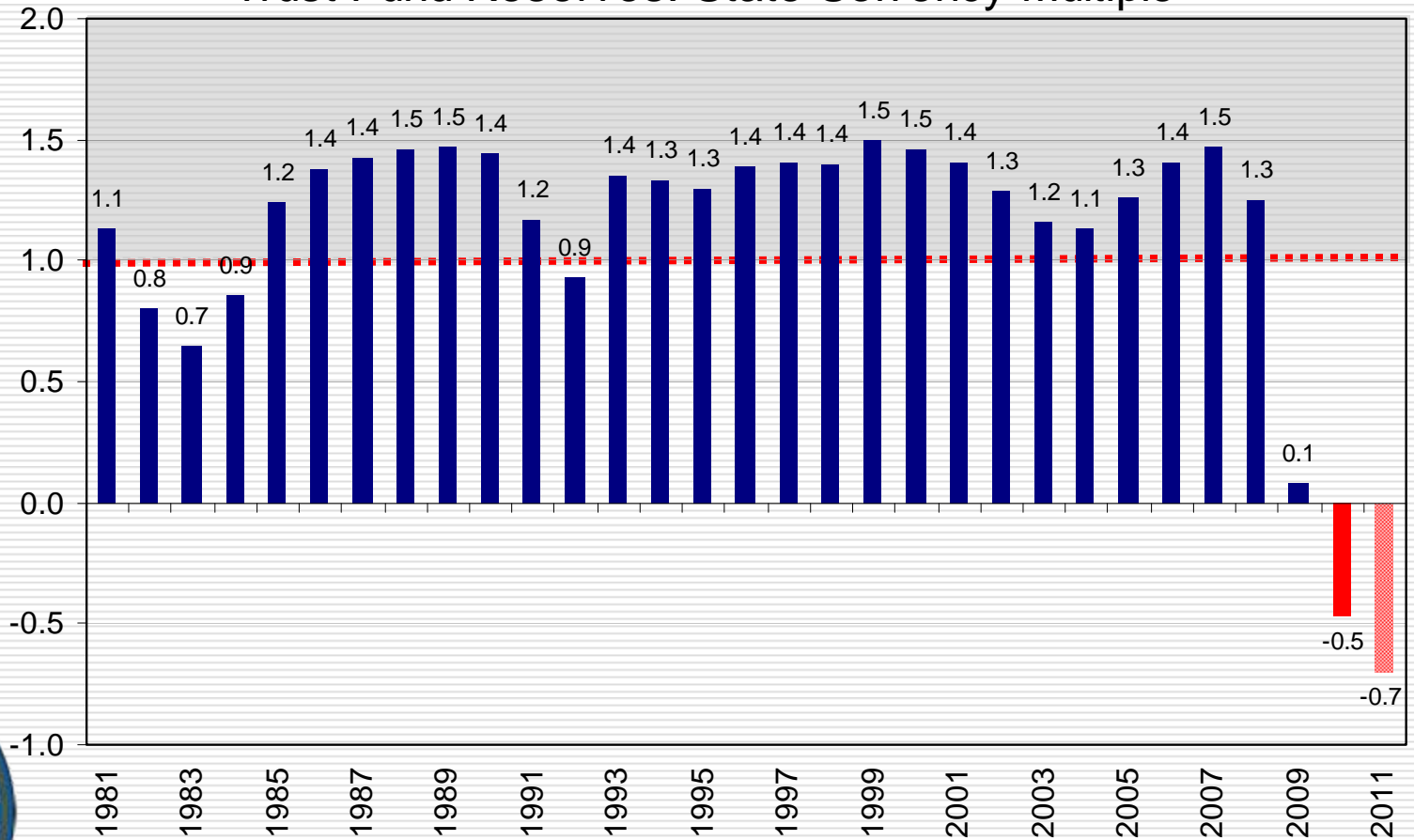
# 2012 Forecast: Historical Solvency Review

<b>Nevada Solvency Calculation</b>	<b>Actual</b>	<b>Actual</b>	<b>Actual</b>	<b>Actual</b>	<b>Preliminary</b>
<b>NRS 612.550</b>	<b><u>2007</u></b>	<b><u>2008</u></b>	<b><u>2009</u></b>	<b><u>2010</u></b>	<b><u>2011</u></b>
Covered Employment	1,116,968	1,114,746	1,058,165	956,818	946,163
Highest Risk Ratio	11.03%	11.03%	14.72%	18.98%	18.98%
Highest Weeks Duration	15.76	15.76	16.26	19.12	19.12
Average Weekly Payment	\$282.01	\$289.25	\$310.74	\$320.69	\$308.26
<b>Solvency Target (Millions)</b>	<b>\$547.6</b>	<b>\$560.5</b>	<b>\$787.0</b>	<b>\$1,113.5</b>	<b>\$1,058.4</b>
<b>UI Trust Fund Level: October - September</b>					
<b>Beginning Fund Balance (Millions)</b>	<b>\$706.9</b>	<b>\$803.1</b>	<b>\$703.4</b>	<b>\$60.6</b>	<b>(\$525.7)</b>
Intake to Fund	400.6	379.1	411.0	267.6	374.3
Taxes	364.5	349.3	305.4	267.6	374.3
UI Mod Incentive	0.0	0.0	76.9	0.0	0.0
Interest	36.1	29.8	28.7	0.0	0.0
Payout From Fund	304.4	478.8	1,053.8	853.9	584.9
Regular Benefits	304.4	478.3	1,025.2	853.9	584.9
Designated Reed Act Funds	0.0	0.5	28.6	0.0	0.0
Net Change in Fund	96.2	(99.7)	(642.8)	(586.3)	(210.6)
<b>Ending Fund Balance (Millions)</b>	<b>\$803.1</b>	<b>\$703.4</b>	<b>\$60.6</b>	<b>(\$525.7)</b>	<b>(\$736.3)</b>
<b>Solvency Level (Millions)</b>	<b>255.5</b>	<b>142.9</b>	<b>(726.4)</b>	<b>(1,639.2)</b>	<b>(1,794.7)</b>
Multiple	1.47	1.25	0.08	-0.47	-0.70
Average High Cost Multiple	1.07	0.91	0.05	-0.75	-0.92
<b>Average Tax Rate</b>	<b>1.38%</b>	<b>1.33%</b>	<b>1.33%</b>	<b>1.33%</b>	<b>2.00%</b>



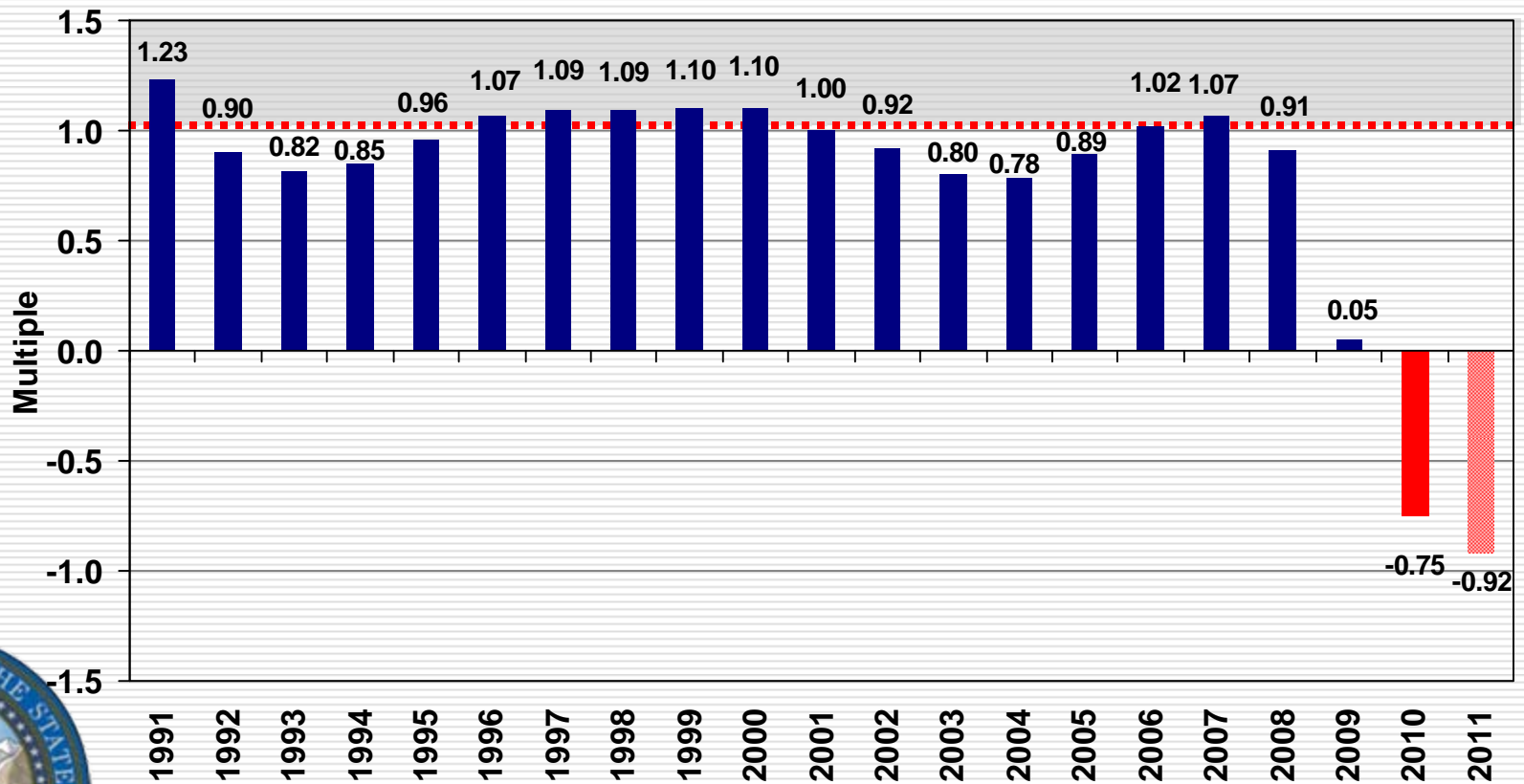
# 2012 Forecast: State Solvency Measure

Trust Fund Reserves: State Solvency Multiple



# 2012 Forecast: AHCM Solvency Measure

Trust Fund Reserves: Average High Cost Multiple





# 2012 Forecast: Potential 2012 Tax Rates

Nevada Solvency Calculation	<u>2012</u>	<u>2012</u>	<u>2012</u>	<u>2012</u>	<u>2012</u>
Covered Employment	947,570	947,570	947,570	947,570	947,570
Highest Risk Ratio	18.98%	18.98%	18.98%	18.98%	18.98%
Highest Weeks Duration	19.12	19.12	19.12	19.12	19.12
Average Weekly Payment	\$300.00	\$300.00	\$300.00	\$300.00	\$300.00
<b>Solvency Target (Millions)</b>	<b>\$1,031.6</b>	<b>\$1,031.6</b>	<b>\$1,031.6</b>	<b>\$1,031.6</b>	<b>\$1,031.6</b>
<b>UI Trust Fund Level</b>					
<b>Beginning Fund Balance (Millions)</b>	<b>(\$736.3)</b>	<b>(\$736.3)</b>	<b>(\$736.3)</b>	<b>(\$736.3)</b>	<b>(\$736.3)</b>
Intake to Fund	449.0	485.4	520.8	556.1	591.5
Taxes	431.2	467.6	503.0	538.3	573.7
FUTA Offset Loan Repayment	17.8	17.8	17.8	17.8	17.8
Payout From Fund	579.4	579.4	579.4	579.4	579.4
Regular Benefits	579.4	579.4	579.4	579.4	579.4
Designated Reed Act Funds	0.0	0.0	0.0	0.0	0.0
Net Change in Fund	(130.4)	(94.0)	(58.6)	(23.3)	12.1
<b>Ending Fund Balance (Millions)</b>	<b>(\$866.7)</b>	<b>(\$830.3)</b>	<b>(\$794.9)</b>	<b>(\$759.6)</b>	<b>(\$724.2)</b>
Solvency Level (Millions)	(1,898.3)	(1,861.9)	(1,826.5)	(1,791.2)	(1,755.8)
Solvency Multiple	-0.84	-0.80	-0.77	-0.74	-0.70
Average High Cost Multiple	-1.07	-1.03	-0.98	-0.94	-0.90
<b>Average Tax Rate</b>	<b>2.00%</b>	<b>2.25%</b>	<b>2.50%</b>	<b>2.75%</b>	<b>3.00%</b>
<b>Average Cost Per Employee at Taxable Wage Base</b>	<b>\$528.00</b>	<b>\$594.00</b>	<b>\$660.00</b>	<b>\$726.00</b>	<b>\$792.00</b>



# 2012 Forecast: Long Term Effect of Different Rates

(\$ in Millions)	2.00%	2.25%	2.50%	2.75%	3.00%
Year of Max Borrowing	2014	2013	2012	2012	2012
Year of Max Offset	2015-17	2015-16	2014-15	2014-15	2013-14
Capped FUTA Years	2016-17	2016	2015	2015	2014
Year Loans are Repaid	2018	2017	2016	2016	2015
Year AHCM reaches 1.0	2021	2020	2019	2018	2017
Maximum Borrowing	\$1,007.0	\$936.5	\$888.9	\$888.9	\$888.9
Total Interest Expense	\$211.9	\$169.1	\$137.6	\$111.8	\$94.5
Total FUTA Offsets	\$463.7	\$369.7	\$270.2	\$270.2	\$164.4
Maximum FUTA Increase	1.5%	1.5%	1.2%	1.2%	0.9%
Loan Repayment from FUTA	46%	39%	30%	30%	18%

- ❑ Table assumes Nevada takes no action to reduce solvency, and avoids the BCR Add-On credit reduction
- ❑ Average time from end of one recession to start of the next during the last 50 years: 5.4 years (December 2014)



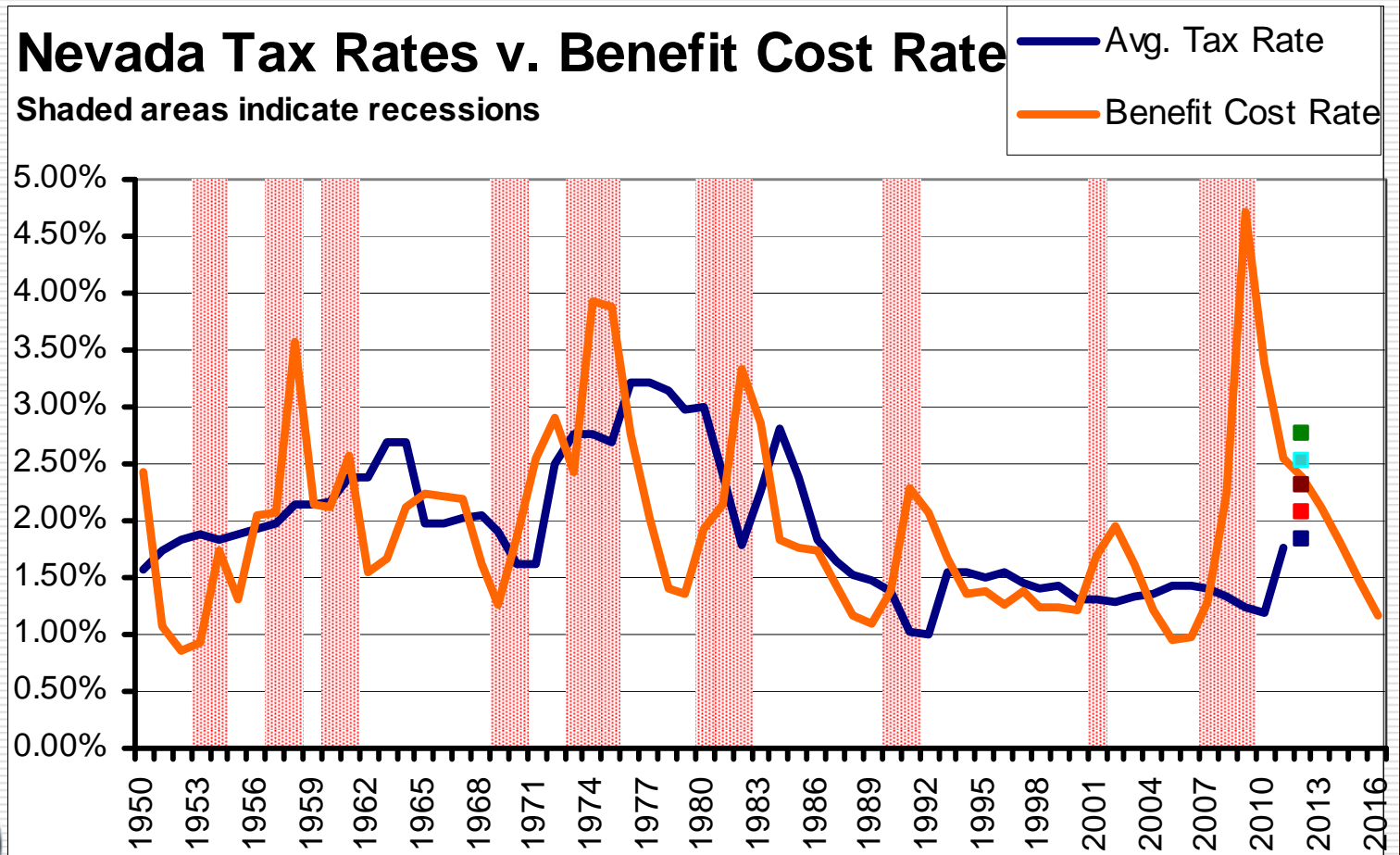
# 2012 Forecast: Estimated Interest Expenses

(\$M)	Title XII Interest Expense at Various Tax Rates				
	2.00%	2.25%	2.50%	2.75%	3.00%
2012	\$38.5	\$37.8	\$37.1	\$36.5	\$35.9
2013	\$43.5	\$40.4	\$37.3	\$34.3	\$31.3
2014	\$43.5	\$37.8	\$32.2	\$26.6	\$21.0
2015	\$39.2	\$30.9	\$22.6	\$14.4	\$6.4
2016	\$30.2	\$19.1	\$8.2	N.A.	N.A.
2017	\$17.1	\$3.2	N.A.	N.A.	N.A.
<b>Total</b>	<b>\$211.9</b>	<b>\$169.1</b>	<b>\$137.6</b>	<b>\$111.8</b>	<b>\$94.5</b>

- ❑ 2012 will be the first year interest accrues for a full 12 months.
- ❑ Table assumes that tax rates and interest rates are fixed.



# 2012 Forecast: Potential 2012 Rates vs. BCR



# 2012 Forecast: Other Considerations

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- ❑ How long will it take the economy to recover?
  - ❑ Average time from end of one recession to beginning of new recession over the last 50 years: 5.4 years
  - ❑ Increasing economic headwinds?
- ❑ What sort of actions might the Federal Government take?
  - ❑ Relief to state Trust Funds or interest obligations?
  - ❑ Implementation of solvency requirements for incentive funds?
  - ❑ Changes to FUTA tax rates or wage base?

