POLICY: **EMPLOYMENT SECURITY SYSTEM FUNDING**

COMMITTEE: **LABOR AND ECONOMIC DEVELOPMENT**

TYPE: **DRAFT**

~~The nation's~~State legislators recognize the many challenges facing the nation as the economy and labor market change~~labor force and workplace change~~. In the states, differing circumstances reflect a changing economic base, prolonged higher unemployment, unique demographic trends, and limitations on available resources. State employment security, unemployment and labor market information systems must figure prominently in efforts to serve the workers and businesses of a 21st century economy.

The National Conference of State Legislatures (NCSL) believes that changes are needed in employment security financing to provide a stable system that will be able to address economic and competitive challenges. NCSL supports decisions aimed at reaching consensus among workers, employers, and state and federal entities to develop comprehensive recommendations for Congress to address the following priorities and inadequacies in the current system.

Trust Fund Solvency

State governments collect payroll taxes from employers to pay for unemployment insurance benefits. These taxes are deposited into state unemployment insurance trust fund accounts in the federal Unemployment Trust Fund where each state, plus the District of Columbia, Puerto Rico and the U.S. Virgin Islands, has its own account. Each state may borrow from the federal account to cover benefits during economic downturn. During the current recession many states have borrowed to cover benefits. These loans must be repaid with interest unless repaid within a short period established in federal law. If states are unable to repay the loan with interest, an automatic gradual increase of the federal tax will be imposed on the state's employers. More than half of the states have already borrowed and the U.S. Department of Labor projections show that up to 40 states are expected to be borrowing by the end of 2010. NCSL is encouraged by recent federal action that provided a waiver of interest payments to states with outstanding federal unemployment loans. However, the waiver expires on December 31, 2010. NCSL urges Congress to immediately extend the deadline on the waiver to states that borrow so that they may continue to pay benefits owed to unemployed workers.

Extended Benefits

Extended benefits are paid by state unemployment insurance agencies from state unemployment accounts but reimbursed at 50 percent from the extended unemployment account. Congress provided extended benefits on a 100 percent federally funded basis several times as a result of the recent recession. NCSL supports an extension of benefits fully funded by the federal government during recessions as a means of stabilizing the economy. NCSL further urges development of more effective triggers for the federal –state extended benefit programs to improve the program's responsiveness during recessions and decrease the need for separate and additional emergency extended benefit programs in periods of high unemployment.

Federal Unemployment Tax Act

Under the framework of the system outlined in the Federal Unemployment Tax Act (FUTA), states collect a state payroll tax to finance unemployment benefits. ~~and the IRS collects a federal payroll tax to provide funds for administration of both the federal and the state systems.~~ The federal treasury holds the collected taxes in 'trust' accounts~~.~~, ~~The amount being collected is more than adequate to fund administrative costs, but the amount returned to the states for administration has been shrinking because these funds~~ but these accounts are included in the federal unified budget ~~and are subject to the appropriations process every year~~. ~~In recent years, states have received an average of a 50-cent return on every dollar collected. State legislators in many states have been forced to add a surtax to employer taxes or to appropriate general fund revenues, or do both, to replace the $3.998 billion confiscated by the Congress in FY06. The remaining accumulated 'trust' funds serve as a "paper" offset to deficits or as an enhancement to federal budget surpluses.~~ NCSL urges the federal government to move the dedicated FUTA trust fund from the discretionary side to the mandatory side of the federal budget and not use the funds to offset the federal budget deficit.

~~Legislators are concerned that the percentage of unemployed workers receiving unemployment insurance benefits has dropped dramatically, and that state unemployment insurance agencies have experienced reduced funding appropriated by Congress in recent years.~~

Administrative Funds

The IRS collects a federal payroll tax from employers to provide funds for administration of both the federal and state unemployment insurance systems. Rising unemployment ~~claims have~~ has resulted in increased state administrative costs and workforce challenges in administering and monitoring the regular, and especially, the extended benefits programs, which have not been sufficiently funded by the federal government. In addition, state unemployment insurance programs have been chronically underfunded in staffing and technology. NCSL urges Congress to adequately fund state administrative functions, and continue the state legislative role in the appropriation of administrative funds.

~~Reed Act~~

~~The Reed Act requires that funds exceeding a statutory ceiling in federal accounts be transferred back to state unemployment trust funds proportional to the state's contribution. Program flexibility has also been reduced by restrictions on Reed Act funds, which can only be used for administering the unemployment compensation law. NCSL believes that Tthese funds should be distributed to the states pursuant to the original intent of the Reed Act~~. ~~with maximum flexibility to also support the Employment Security System~~.

~~NCSL therefore supports legislation recently introduced in Congress that will strengthen the unemployment insurance system by using $7 billion in revenue from the federal unemployment insurance surtax to provide reimbursements to states that modernize their programs by improving benefits for unemployed workers who have fallen through~~

~~the cracks of the unemployment insurance system. The legislation also provides $500 million shared by all states for additional unemployment insurance administrative funding.~~

~~NCSL therefore urges the following reforms:~~

- ~~Moving the dedicated FUTA trust fund from the discretionary side to the mandatory side of the federal budget.~~
- ~~Adequate funds for state administrative functions.~~
- ~~Use the 'temporary' surcharge for benefit improvements for unemployed workers.~~
- ~~Adherence to the provisions of the Reed Act that guarantee that surplus funds be returned to the states.~~
- ~~A continuation of the state legislative role in the appropriation of administrative funds.~~

~~Further, legislation enacted in more than forty states imposes new penalties on employers that seek to avoid paying their fair share of unemployment tax in order to eliminate the practice called SUTA dumping (standing for "state unemployment tax avoidance"). NCSL believes that SUTA dumping negatively impacts state unemployment insurance trust funds and shifts the tax burden to law-abiding employers who then pay more than their fair share when SUTA dumping is not addressed under current law. In keeping with the shared nature of the national unemployment insurance program, NCSL believes the states and federal government should continue to act collaboratively to curb these abuses.~~