Unemployment Compensation in Ohio: Making it Solvent and Modernizing it

Legislative Briefing

April 21, 2010

Why Unemployment Compensation Is Important

- UC benefits represent a first line of defense against wage loss and poverty.
- UC benefits stimulate our economy--$1.61 in added growth for every dollar of UC.

Basics of Unemployment Compensation

- Federal/state partnership since Social Security Act of 1935
- Federal taxes of 0.8% on first $7,000 of each employee’s pay, or $56 per year, supports administration of the system, loans to states and extended benefits
- Employer taxes support state trust fund. These taxes are a function of how much the employer has paid into the fund, and how much laid-off workers from the employer have gotten in benefits – range of rates this year from 0.5% to 9.4% on the first $9,000 in earnings, or $45 to $846 per worker -- $266 on average
- Benefits paid to workers who meet certain requirements. They receive half of their previous pay, up to a maximum that depends on the number of dependents. The average weekly benefit last year in Ohio was $321

UC benefits in Ohio

- More than half a million Ohioans received unemployment compensation during 2009, or an average of close to 200,000 a week
- State UC benefits pumped more than $3.1 billion into Ohio’s economy last year

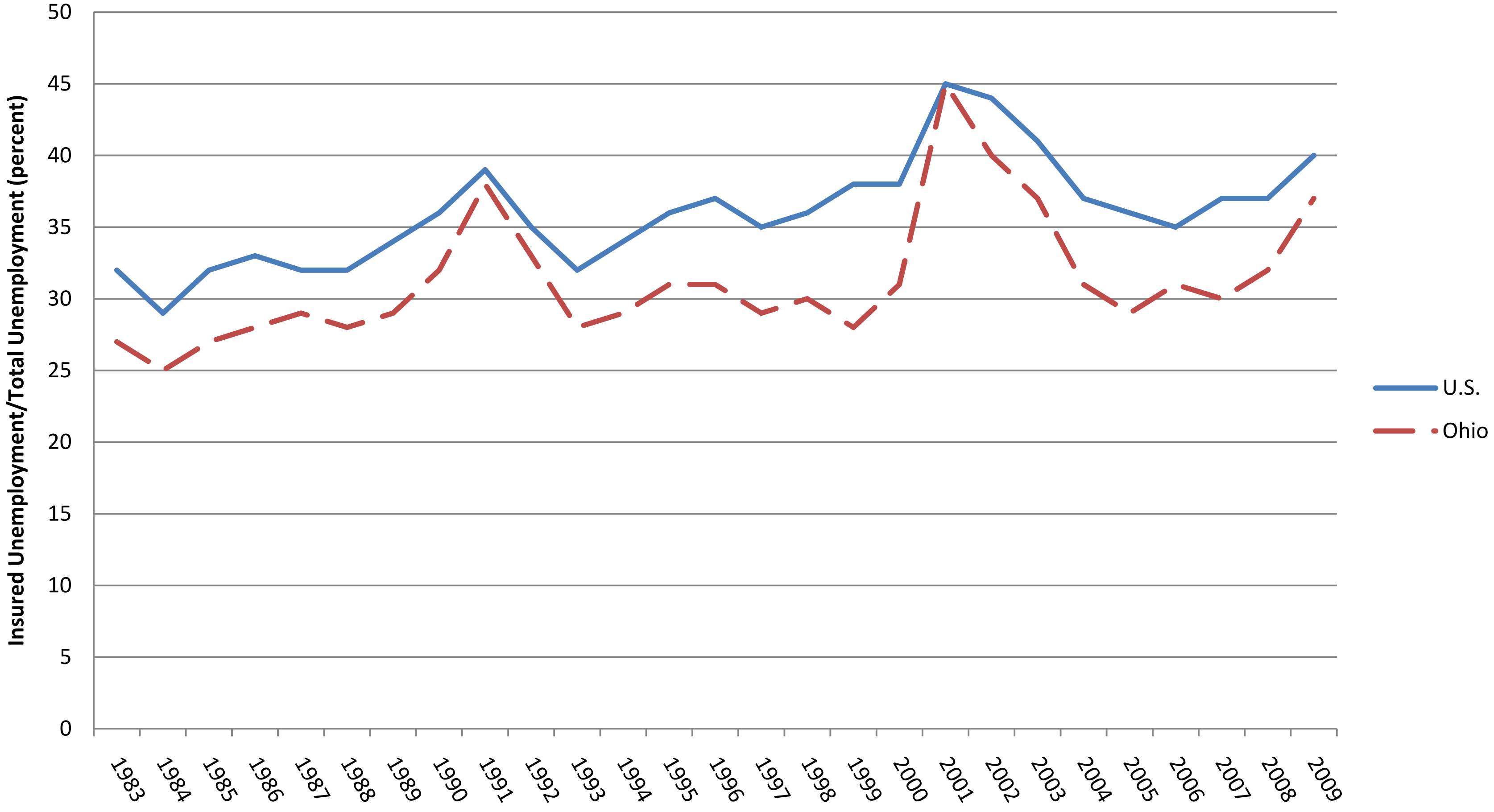
People are unemployed longer

- Last year, 247,778 exhausted their regular Ohio unemployment benefits
- On average, jobless workers are receiving state benefits for more than 21 weeks—higher than any time in decades (at least since 1970)
- More than half of those getting unemployment benefits in Ohio are receiving them because of the federal extended benefit program

A negative aspect of Ohio's system

- Ohio has among the most stringent earnings requirements in the country to qualify for UC.
- Ohio is one of only three states where a worker making the minimum wage for 29 hours a week, or someone making $10 an hour and working 20 hours a week, cannot qualify.
- This is one reason why fewer jobless Ohioans collect unemployment benefits than do those in most other states – we rank 43rd

Share of unemployed receiving state benefits



What is UI Modernization?

- American Recovery & Reinvestment Act offered federal incentives of $7 billion to states that improve their UI systems. Not counting states that acted since January, 32 states have been approved to receive $2.8 billion so far
- Ohio qualified for a third of its share -- $88.2 million – because it already allowed workers to count their most recent earnings to qualify for benefits (known as the alternative base period).

Ohio - UI Modernization Options

To gain another $176.3 million in federal incentives, Ohio must enact 2 of 4 added UI modernization elements by August 2011:

– Part-time eligibility -- UI in training
– Dependency allowance -- Family quits

Part-time eligibility

- Jobless workers who earned majority of wages in part-time work must be eligible for UC
- Part-time workers must still meet the same earnings requirements as others
- One in every five Ohio workers works part-time. Seventy percent of part-time workers are women.
- 27 states allow part-timers to qualify

UC In Training

- Ohio has expanded the kinds of training that workers may get and receive regular UC (Governor’s executive order last fall)
- This option means extending benefits while in approved training for 26 weeks
- Extended training allows workers to prepare for new jobs
- 15 states permit such extended benefits

Dependency Allowances

- Now, you have to have earned more than $750 a week to qualify, so jobless workers who need them most can’t get them.
- Ohio could scrap existing system and pay $15 a week per dependent, up to $50 total.
- Alternately, we could keep existing system and add the $15 weekly for those who don’t now qualify
- 6 states follow this option

Compelling family circumstances

- This recognizes that the workplace has changed since 1935. Many states have approved benefits for family-related quits (see numbers in parentheses below).
- It would allow people to get UI if they quit their jobs and:
  - They were victims of domestic violence (31 states & DC);
  - They were caring for a sick or disabled member of their immediate family (24 states); or
  - They were following their spouse to a job located where it is impractical to commute (22 states).

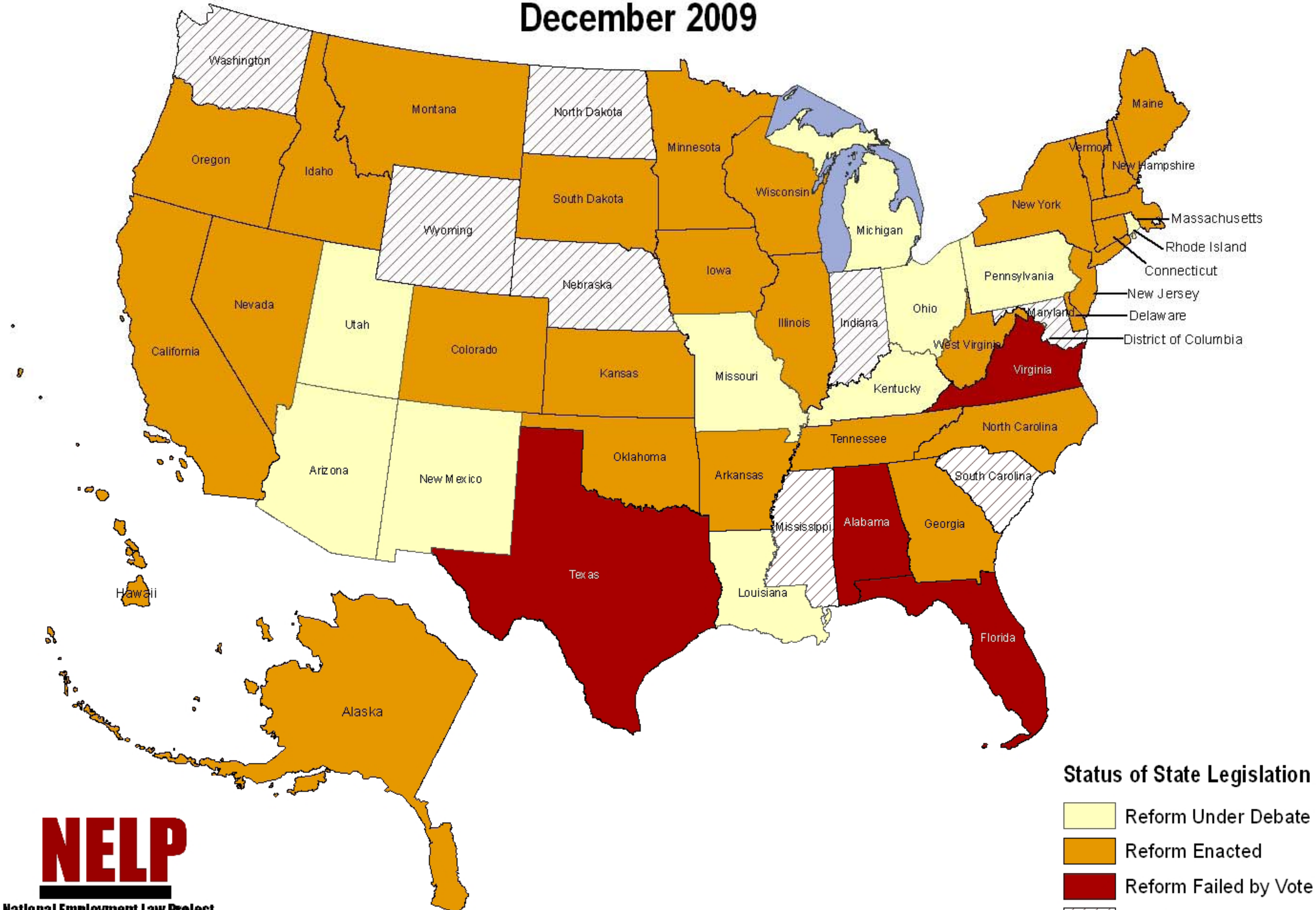
All three are required to qualify for federal funds. Nineteen states have enacted all three of these reforms.

States across the country have approved UI Modernization

- States with Republican governors such as Georgia, Minnesota, Nevada, South Dakota and Utah have approved UI Modernization.
- Last week, the Nebraska legislature passed a bill including extended benefits in training and the alternative base period; it already had part-time eligibility and all of the compelling family reasons.
- When governor of Alaska, Sarah Palin approved legislation for an alternative base period. The state already offered dependency benefits and spousal relocation, and now has made regulatory changes to include the domestic violence and illness provisions

ARRA UI Incentive Funding Reforms: State Activity Status

December 2009



NELP
National Employment Law Project

Cost

- The $176 million would pay for these improvements for several years.
- Wayne Vroman, retained by ODJFS, last year estimated cost of part-time and training together at $38.7 million a year.
- National Employment Law Project estimates cost of part-time and compelling family reasons at $47.2 million.

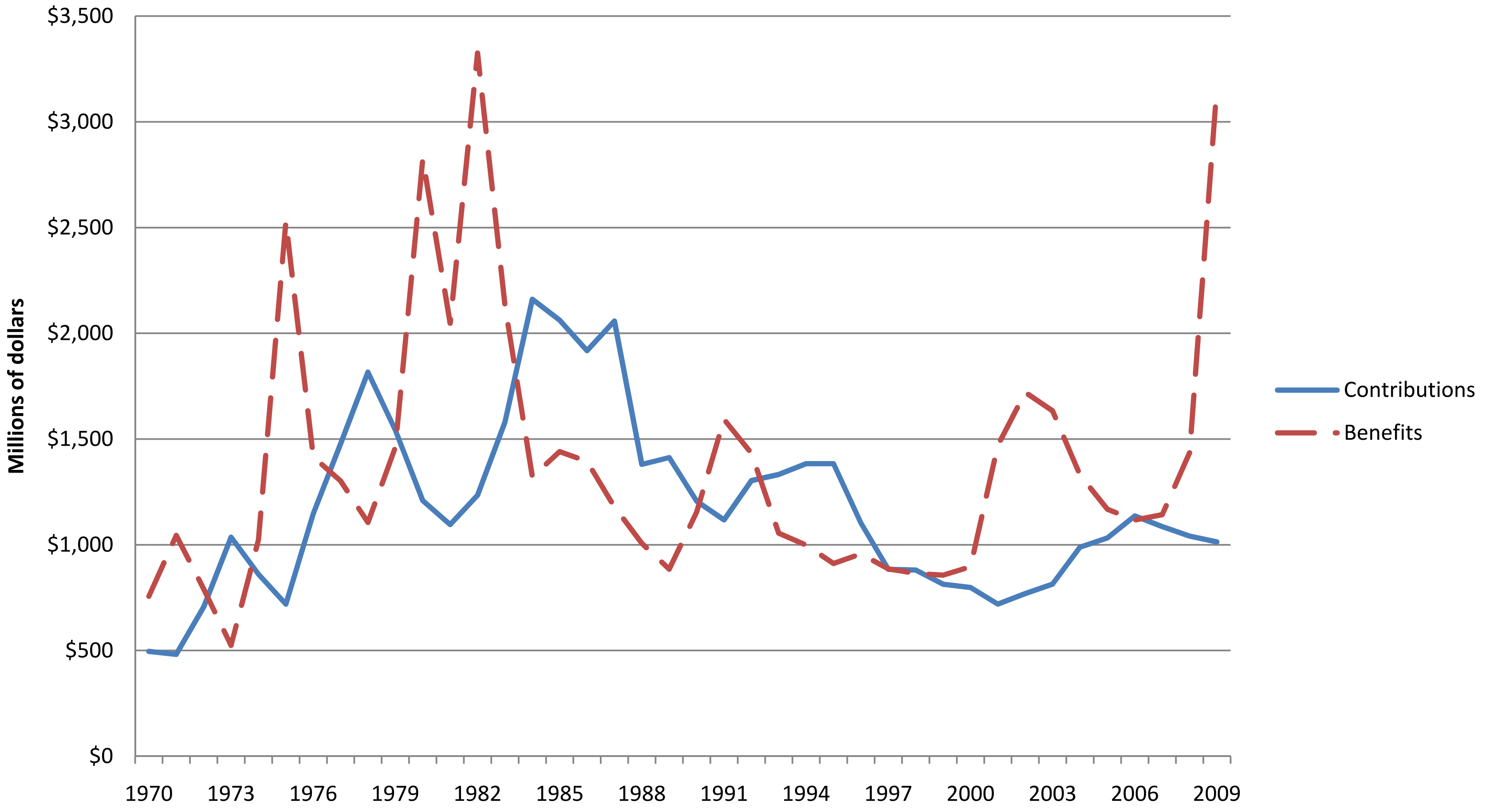
Tax cuts

- Recovery Act money will pay for an even greater share of these benefits when you realize that the $88 million Ohio already received caused an across-the-board tax cut for employers
- It resulted in a reduction of 0.2% for every employer, or $18 per employee. The overall tax schedule in 2010 was reduced or stayed the same for employers in nearly every tax bracket.

Why is the Ohio fund broke?

- Inadequate financing of system for many years
- Ohio is cutting tax rates even when it owes billions of dollars—shows need for overhaul of tax system
- Increases in benefits, mostly because more people are unemployed for longer periods

Taxes and Benefits in Ohio, Adjusted for Inflation



Financing

- Ohio taxes employers on the first $9,000 of each employee’s pay
- Three components:
  - Experience rating of individual employer
  - Mutualized rate – fell in 2010
  - Minimum safe level – maxed out since 2006

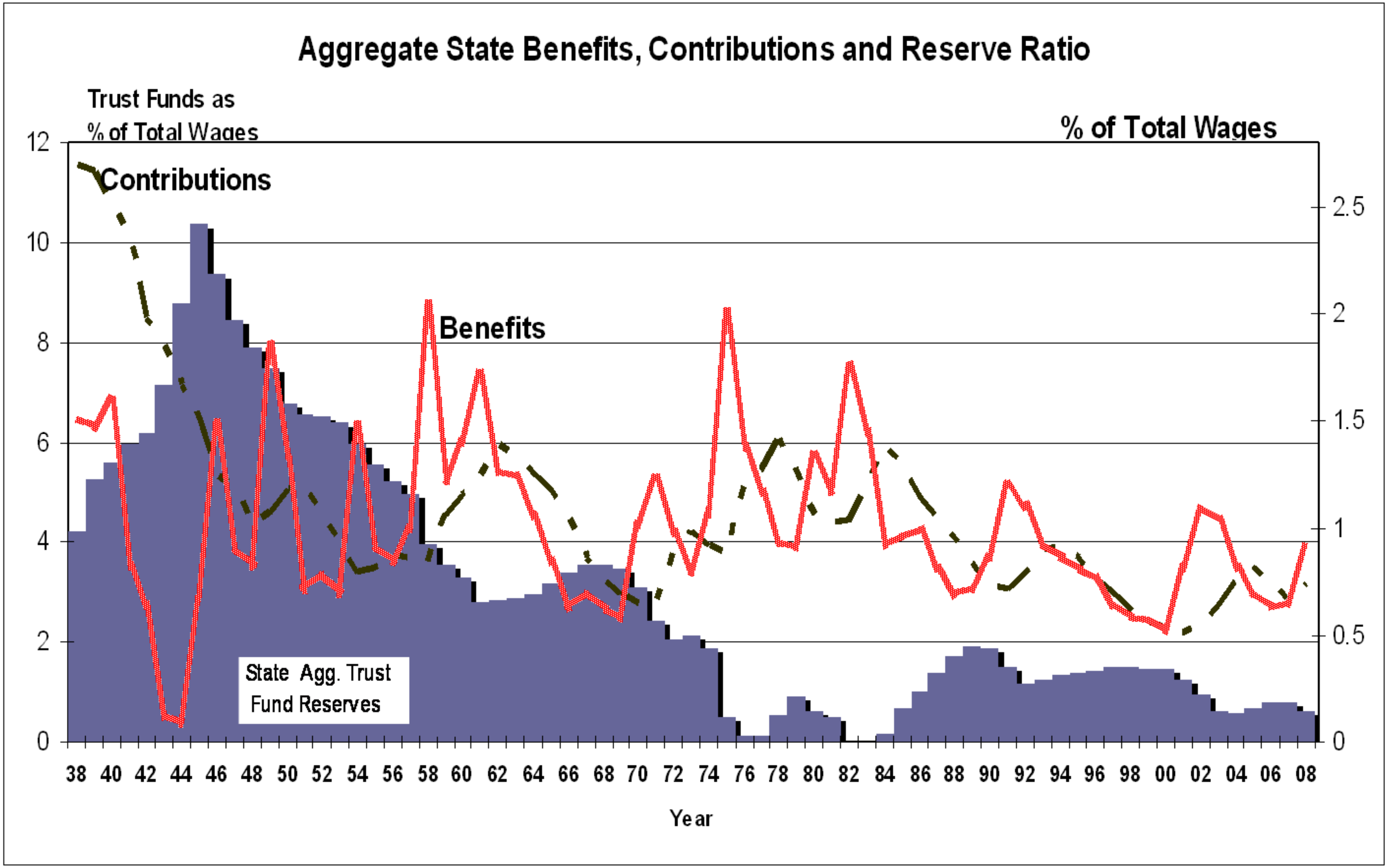
Taxable wage base

- $9,000 in Ohio has not been raised since 1995.
- Average for U.S. is $12,323
- Less than a quarter of Ohio wages are taxed. Under Social Security, approved in the same 1935 act, $106,800 is taxed.
- 16 states index their wage bases, usually to wages.

Pay as you go

- States had $51 billion in their trust funds when the last recession began in 2001; they had only $38 billion at the beginning of the current recession
- Reserves were lower going into this recession than any previously recorded
- States including Ohio have shifted away from “forward financing”

History of UI Financing



Source: U.S. Department of Labor ETA-394 Report

Inadequate financing

For years, the average tax rate nationally has been below the U.S. Department of Labor’s measure of adequate financing

A national problem

- 34 states and the Virgin Islands had borrowed more than $40.7 billion as of April 15.
- Ohio has borrowed $2.29 billion; all of its neighbors except WV have borrowed, too: IN, $1.85 billion; KY, $789 million; MI, $3.87 billion; PA, $2.93 billion
- U.S. Department of Labor estimates by 2102, 40 states will have borrowed $90 billion

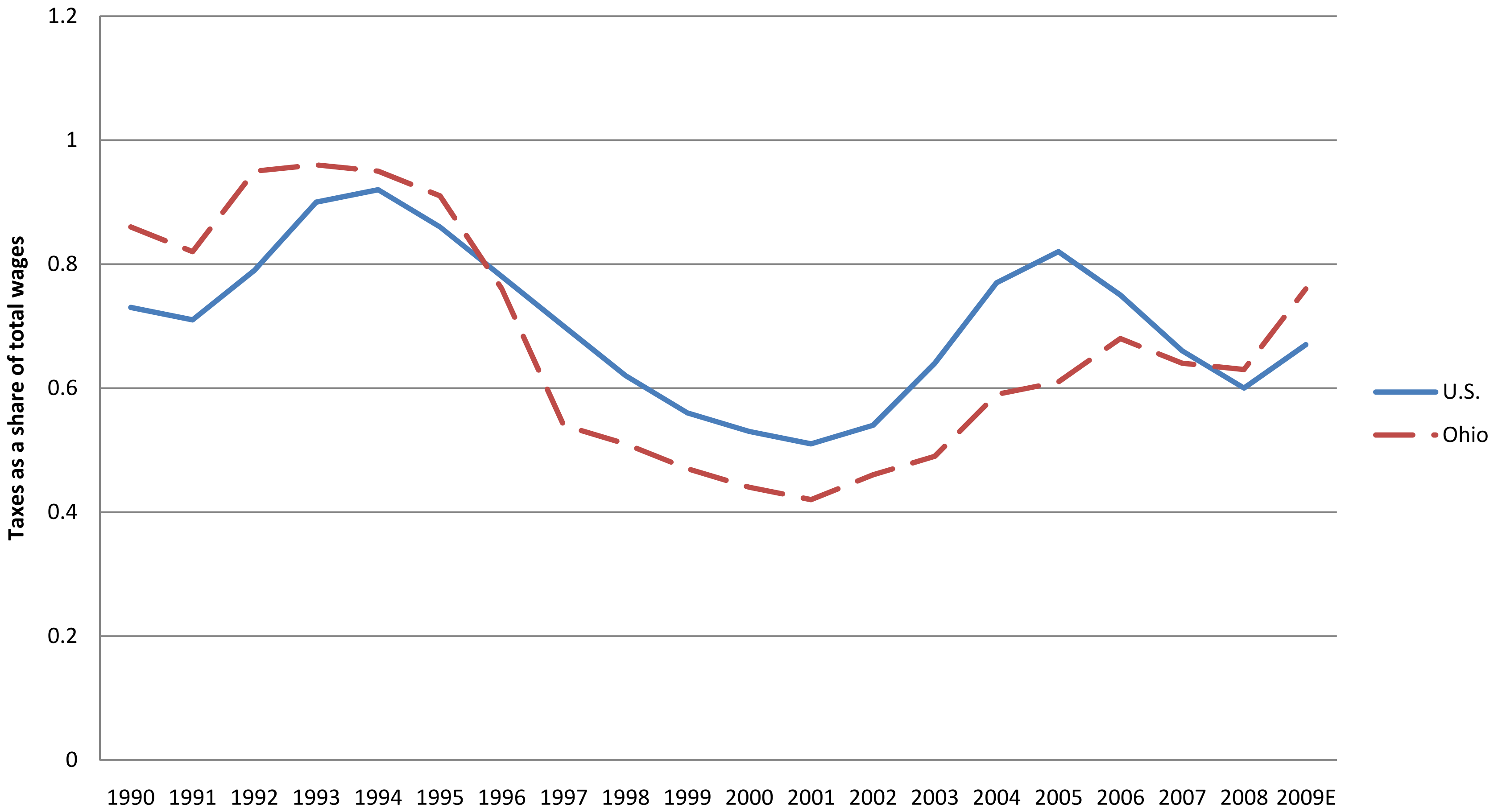
Ohio was going broke *before* benefits soared

"Benefit payments have grown as the economy has grown, but taxes have lagged economic growth."

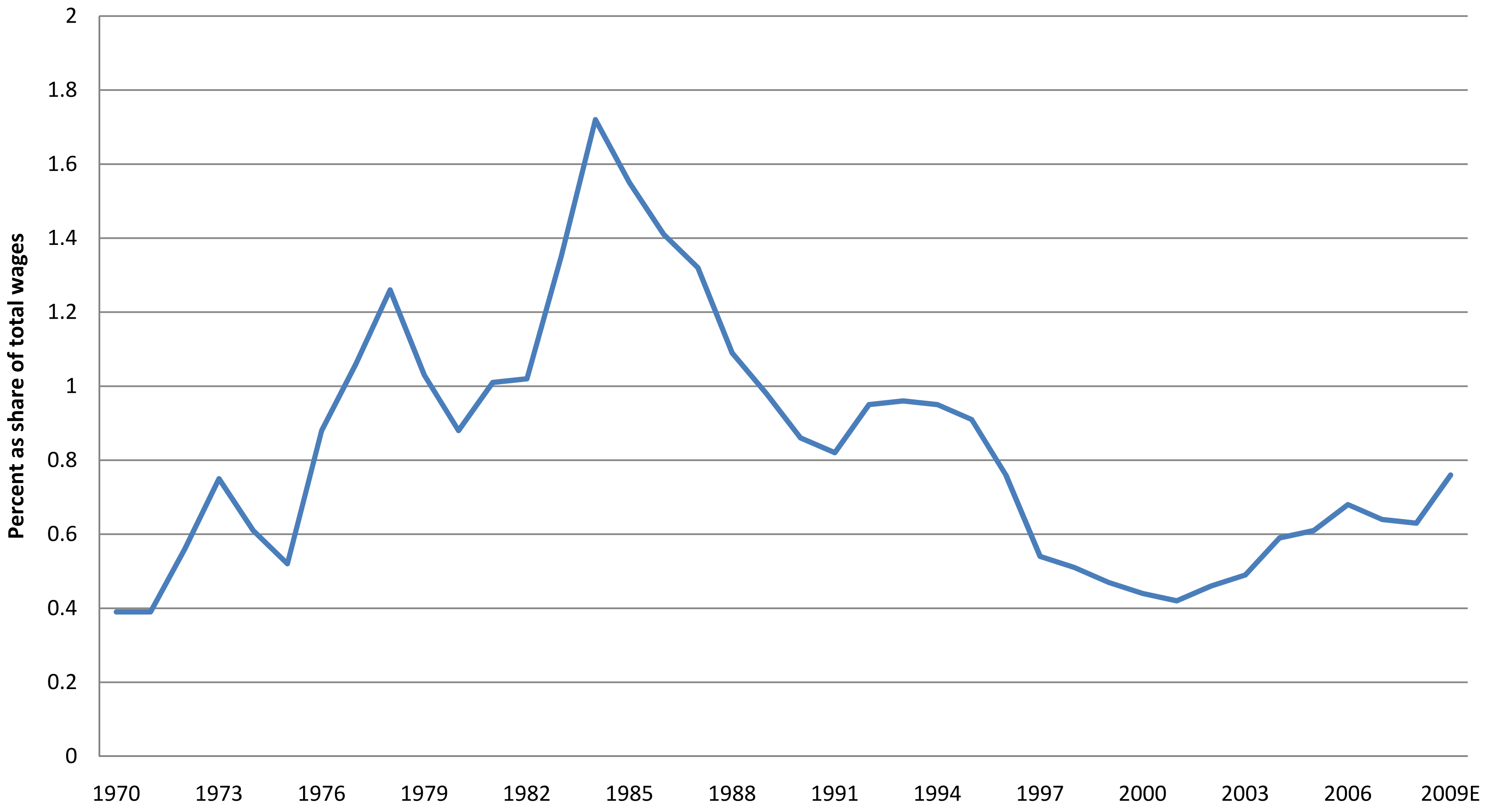
– Wayne Vroman final report to ODJFS, July 10, 2008

Vroman found that reserves had fallen since 2000 mostly because of the limited response of UI taxes, not high benefit payouts.

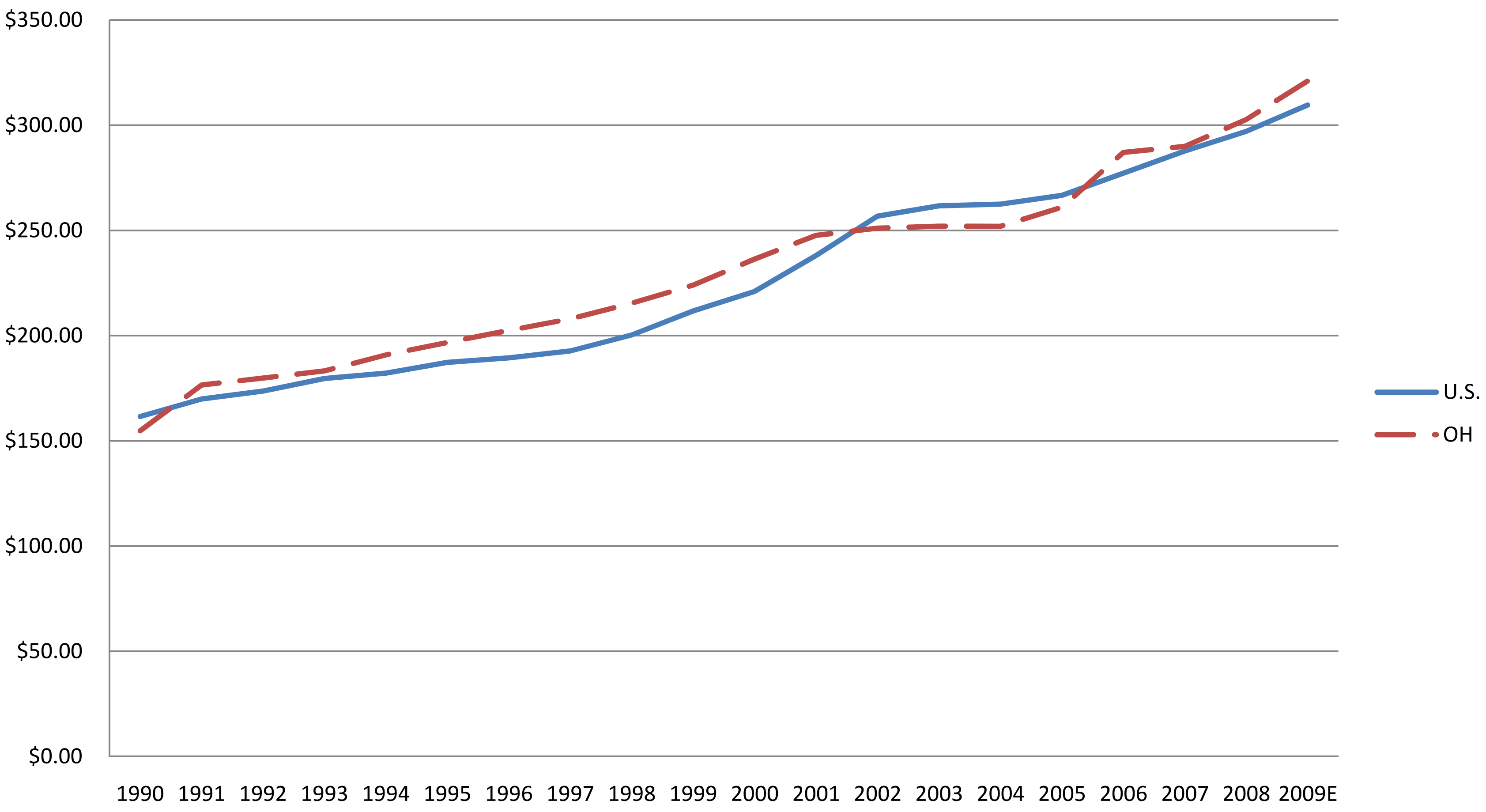
Ohio and U.S. Employer Tax Rates as a Share of Total Wages



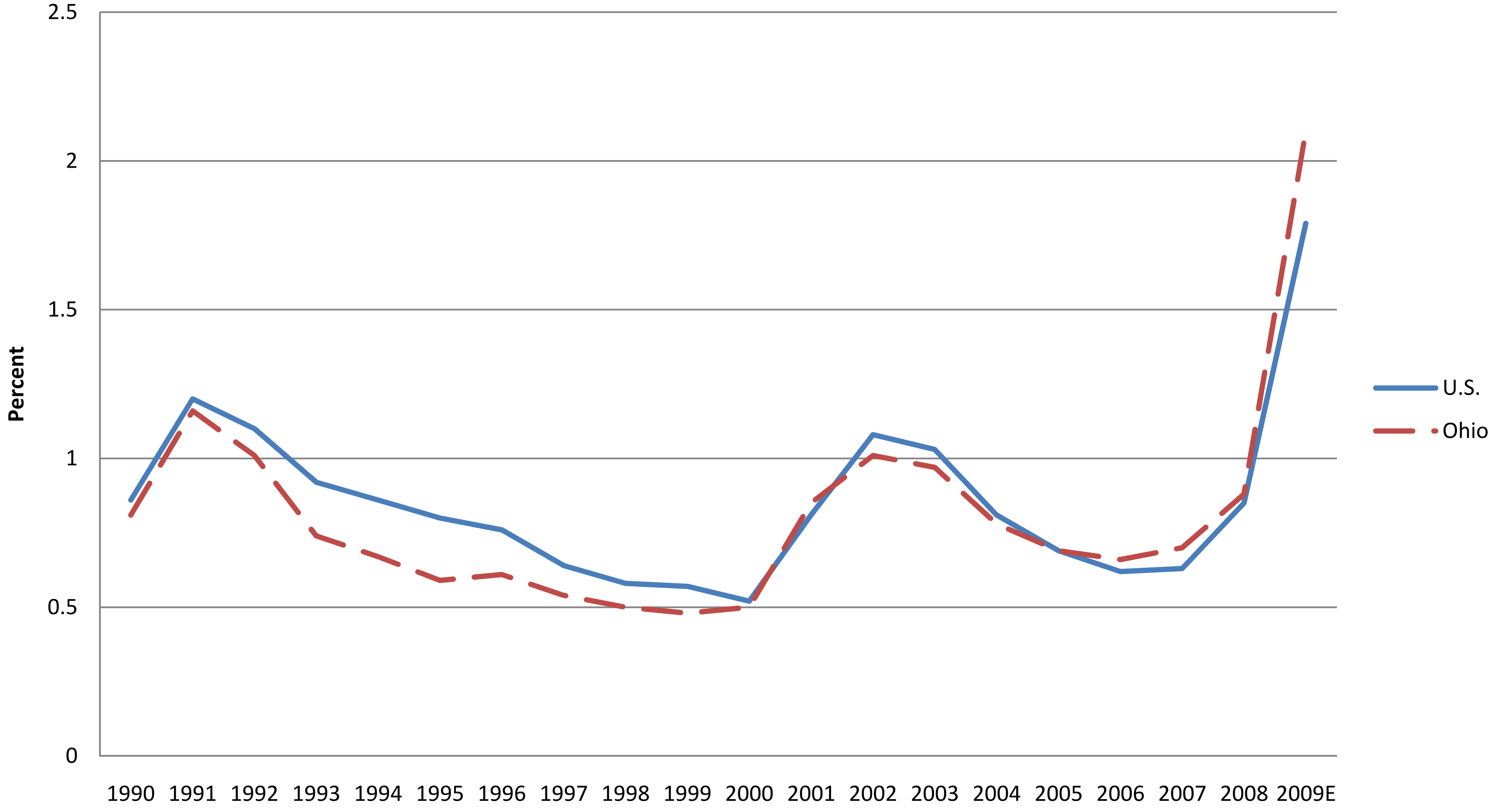
Ohio Employer Tax Rates as a Share of Total Wages, 1970-2009



Average Weekly Benefits



Benefits as a Share of Total Wages



What caused the surge in benefits?

- By far the main reason: An 88% increase in the number of weeks of state unemployment benefits paid last year. More people are unemployed longer.
- A somewhat greater share of unemployed Ohioans is getting state benefits
- Average benefits also increased

Benefit levels are modest

- Nearly four-fifths of Ohioans receiving benefits last year got $372 or less a week
- Annualized, the average weekly benefit of $321 last year is less than the federal poverty standard for a family of three
- Ohio is replacing 41% of the average wage (and remember that many low-wage Ohioans don’t qualify, making this figure higher)

What if Ohio does nothing?

- Debt of an estimated $3 billion by end of year, possibly $7 billion by 2015
- Ohio can continue borrowing from U.S. to pay benefits
- State will have to pay interest on its debt starting next year – about $160 million in CY11. Existing UC taxes cannot be used.
- Starting in January 2012, automatic tax increases on employers to pay debt - $21 per covered employee first year, $42 second year

Proposal

- No automatic tax cuts
- Surtax to pay interest, if necessary
- Phase in a substantial increase in the taxable wage base, and index it to wages
- Support a higher federal taxable wage base and federal relief for states that improve solvency without cutting benefits
- Temporary freeze on increases in maximum benefits (as proposed in 2008)

The Last Time We Went Broke

- In the 1980s, we borrowed from the federal government for eight years
- We paid $263.7 million in interest
- Automatic tax increases for five years, totaling $799 million
- Eligibility tightened, still feeling the effects. Benefit maximums frozen, taxes raised.
- What happens this time will depend in part on what happens in Washington

National picture

- A continued waiver of interest may get support in Congress
- Proposals to give states debt relief should also require higher federal wage base and actions by states to improve their financing without compromising benefits

Conclusions

- Some states, such as Oregon, are solvent
- Insolvency is a product of policy, not just the poor economy
- Ohio should start taking steps to properly fund its UC system, starting with the taxable wage base

For more information:

- Visit the Policy Matters Ohio web page on unemployment compensation at: http://www.policymattersohio.org/publications.htm#unemployment_compensation
- Contact Zach Schiller at Policy Matters Ohio

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