

# **HB 2619: Unemployment Insurance Trust Fund Special Assessment**

Revised: 5-2-11

## The Issue:

Due to higher-than-anticipated job losses in the state, the Arizona Unemployment Insurance Trust Fund became insolvent in 2010. To address the insolvency issue, Arizona borrowed funds from the U.S. Department of Labor (DOL) to continue its ability to pay out unemployment benefits to claimants beginning in early March 2010. Arizona is one of 31 states borrowing from the U.S. DOL.

To that end, the business community supported HB 2619, a plan to stabilize the UI Trust Fund and pay back the loan plus any interest that may have accrued over the life of the loan. The Legislature approved and Governor Brewer signed the bill into law. **The effective date for the bill is July 20, 2011 and the special assessment is scheduled to terminate after December 31, 2012.**

## Overview of the Unemployment Insurance system

The unemployment insurance (UI) system was created out of a social contract between employers and employees. Through UI, employers insure their employees against temporary income loss due to a loss of a job. Because UI is a payroll cost to employers, the system is designed to strike a balance between employee protections and affordability to employers.

Both Arizona and the federal government are responsible for UI. Under the Federal Unemployment Tax Act (FUTA), the federal government imposes a tax on employers across the U.S. at a rate of 6.2%. However, because Arizona has an approved program with the federal government, employers in the state are granted a 5.4% credit against that rate. Therefore, Arizona employers pay a FUTA tax of 0.8%.

The State Unemployment Insurance Act (SUTA) is the state statute which governs the Arizona UI program. Key information about the program includes:

- *Arizona tax rates* – Range from 0.02% (low end) to 5.4% (high end). Each employer is experience rated<sup>1</sup>, with the rate being based on the taxes paid minus the amount of benefits attributable to the business divided by the employer's average annual payroll. This produces an employer's reserve ratio.
- *Taxable wages* – The taxable wage base for calculation of the state UI tax is based on the first \$7,000 of wages per employee per year.
- *Job Training Tax* – Considered a surcharge for the purposes of training workers, it is a 0.1% tax on the first \$7,000 of taxable wages, totaling \$7 per employee per year. The tax is collected by the Arizona Department of Economic Security (DES) and the program is administered by the Department of Commerce.
- *Unemployment Insurance Trust Fund* – The fund is held at the U.S. Treasury and managed by DES. UI collections are deposited into this fund. UI benefits are administered from this fund.
- *Maximum Weekly benefit* - \$240 per week.
- *Eligibility for UI benefits* - Includes being available and actively searching for full time employment.

## Impacts of borrowing

As of October 19, 2010, Arizona has borrowed \$358 million. Of that, \$188 million has been repaid to the U.S. DOL, leaving a \$170 million outstanding balance. It is anticipated that the state will need to borrow additional money into calendar year 2013 to ensure unemployment benefits can be paid to claimants.

Under the American Reinvestment and Recovery Act (ARRA), the feds had opted to waive the interest on the loan for an established time period that recently expired on December 31, 2010. At this time, the federal government has not extended the "interest-free" period. Therefore, DES projects that Arizona and its employers will incur interest charges

---

<sup>1</sup> New employers are not experience rated.

<sup>2</sup> The 2.7% add-on is based on a calculation completed by the U.S. DOL if the state has an outstanding loan balance on November 10<sup>th</sup> of each consecutive year.

<sup>3</sup> The 0.4% and 0.6% assessment on the first \$7,000 of taxable wages provides sufficient additional contributions to address Fund

of between \$12 and \$13 million for calendar year 2011. The interest is based on a rate of 4.6% and is charged to the average daily outstanding balance.

Why the assessment is needed

Failing to pay back the loan plus interest accrued can jeopardize the FUTA credits enjoyed by all Arizona’s employers. According to DES, if Arizona has an outstanding loan balance on November 10, 2012, this state’s employers will begin to lose the FUTA credits. Reductions would start in increments of 0.3% annually. Below, the chart provides a schedule of FUTA offset credit reductions if the loan plus interest is not repaid by its scheduled due date.

YEAR	Basic FUTA increase	Additional FUTA increase	Potential FUTA Rate
2011	0.0%	0.0%	0.8%
2012	0.3%	0.0%	1.1%
2013	0.6%	Up to 2.7% add-on <sup>2</sup>	1.4% min. (up to 4.1%)
2014	0.9%	Up to 2.7% add-on	1.7% min. (up to 4.4%)

The final outcome, HB 2619 becomes law

Universally, the stakeholders agreed that failure to act would have led to long-term harm. Therefore, the stakeholders supported **HB 2619**, a bill that received support from both the Legislature and Governor Brewer. The new law provides for a temporary assessment of 0.4 percent in 2011 and 0.6 percent in 2012 on all employers. The assessment rate is applied to the first \$7,000 of taxable wages for each employee. The UI special assessment will go to repay the loan plus accrued interest, as well as stabilize the UI Trust Fund.

Below, the chart breaks down the costs per employee, with an assessment of 0.4 percent in 2011 and 0.6 percent in 2012. It also assumes a timely loan and interest repayment, no loss of FUTA credits, and a gradual economic recovery.

	CY 2010	CY 2011	CY 2012	CY 2013	Total Cost per Employee over the time period
FUTA Tax	\$56	\$56	\$56	\$56	\$224
Az UI Tax	\$146	\$157	\$161	\$161	\$625
Assessment <sup>3</sup>	\$0	\$28	\$42	\$0	\$70
<b>Sub-Total</b>	<b>\$202</b>	<b>\$241</b>	<b>\$259</b>	<b>\$217</b>	<b>\$919</b>
Job Training Tax	\$7	\$7	\$7	\$7	\$28
<b>TOTAL</b>	<b>\$209</b>	<b>\$248</b>	<b>\$266</b>	<b>\$224</b>	<b>\$947</b>

<sup>2</sup> The 2.7% add-on is based on a calculation completed by the U.S. DOL if the state has an outstanding loan balance on November 10<sup>th</sup> of each consecutive year.

<sup>3</sup> The 0.4% and 0.6% assessment on the first \$7,000 of taxable wages provides sufficient additional contributions to address Fund solvency while avoiding the loss of FUTA credits. This would amount to \$28 per employee for the 0.4% assessment; and \$42 per employee for the 0.6% assessment.

Impact to employers: a comparison of implementing HB 2619 verses no legislative action

Below, the first chart demonstrates the impacts of HB 2619 to the average employer. Had the state Legislature and Governor not taken any legislative action that allowed for the repayment of the loan and interest, employers would have experienced increased costs per employee over the long-term (see second chart on the next page).

As shown below and on the following page, the assessment in calendar year (CY) 2011 will raise the overall cost of an average employer’s unemployment insurance annual obligation by \$28 per employee. In CY 2012, the cost difference between HB 2619 and the “no legislative action” approach shrinks to a \$21 per employee. Once the assessment sunsets after December 31, 2012 - assuming the federal loan plus interest is repaid by November 2012, the average employer will see a cost savings of \$231 per employee over the “no legislative action” approach. By CY 2014, the average employer will see a cost savings of \$252 over the “no legislative action” approach. Over a five-year time-period, HB 2619 will have helped the average employer save \$434 over the “no legislative action” approach.

<b>CHART #1: With the passage of HB 2619</b>						
	CY 2010	CY 2011	CY 2012	CY 2013	CY 2014	Total Cost per Employee over the time period
FUTA Tax	\$56	\$56	\$56	\$56	\$56	\$280
Az UI Tax <sup>4</sup>	\$146	\$157	\$161	\$161	\$161	\$786
Assessment <sup>5</sup>	\$0	\$28	\$42	\$0	\$0	\$70
<b>Sub-Total</b>	<b>\$202</b>	<b>\$241</b>	<b>\$259</b>	<b>\$217</b>	<b>\$217</b>	<b>\$1136</b>
Job Training Tax	\$7	\$7	\$7	\$7	\$7	\$35
<b>TOTAL</b>	<b>\$209</b>	<b>\$248</b>	<b>\$266</b>	<b>\$224</b>	<b>\$224</b>	<b>\$1171</b>

<sup>4</sup> The average rate by employers per employee: 2% in 2010, 2.2% in 2011, 2.3% in 2012, 2.3% in 2012. The rate band runs from 0.02 (no claims/positive reserve ratio) to 5.4 (high claims/negative reserve ratio).

<sup>5</sup> The 0.4% and 0.6% assessment on the first \$7,000 of taxable wages provides sufficient additional contributions to address Fund solvency while avoiding the loss of FUTA credits. This would amount to \$28 per employee for the 0.4% assessment; and \$42 per employee for the 0.6% assessment.

<b>CHART #2: “No legislative action” approach</b>						
	CY 2010	CY 2011	CY 2012	CY 2013	CY 2014	Total Cost per Employee over the time period
FUTA Tax	\$56	\$56	\$77 <sup>6</sup>	\$287 <sup>7</sup>	\$308 <sup>8</sup>	\$784
Az UI Tax <sup>9</sup>	\$146	\$157	\$161	\$161	\$161	\$786
Assessment	\$0	\$0	\$0	\$0	\$0	\$0
<b>Sub-Total</b>	<b>\$202</b>	<b>\$213</b>	<b>\$238</b>	<b>\$448</b>	<b>\$469</b>	<b>\$1570</b>
Job Training Tax	\$7	\$7	\$7	\$7	\$7	\$35
<b>TOTAL</b>	<b>\$209</b>	<b>\$220</b>	<b>\$245</b>	<b>\$455</b>	<b>\$476</b>	<b>\$1605</b>

<sup>6</sup> Assuming an unpaid loan to the federal government and a loss of a FUTA credit at 0.3%. It would increase from 0.8% to 1.1%.

<sup>7</sup> Assuming that a loan balance remains, the FUTA credit loss increases by another 0.3% plus a DoL penalty of 2.7%.

<sup>8</sup> Assuming that a loan balance remains for another year, causing future loss of FUTA credits of an additional 0.3% plus a DoL penalty of 2.7%

<sup>9</sup> The AZ UI Tax for the average employer under the “no legislative action” approach assumes that the average employer UI tax rate will track the same as the estimates that were included in determining the average UI tax rate under HB 2619.