

Responding to Recession: Strengthen State Unemployment Insurance Programs

By National Employment Law Project

When states reconvene for their legislative session in January 2009, they will do so with the nation's economy officially in a serious recession. With unemployment claims rising steeply, the states are feeling the blow in the form of increased demand for state services, declining revenues, and severely stressed state budgets. This combination of forces requires state policy makers to make hard choices to maintain safety net programs and support the local economy. What follows is a brief outline of the key role that Unemployment Insurance (UI) can play to help address these concerns as the recession takes its toll in the states.

While Congress and the President debate whether to provide much-needed UI assistance as part of the economic recovery package (in the form of the Unemployment Insurance Modernization Act), the states are also in position to move forward with UI reforms to help fight off the recession. States have already taken action to strengthen their program in anticipation of demands of the recession. If other states follow their lead (building on proposed federal UI measures) they too will be making significant progress toward alleviating the individual and community hardships of the economic slowdown.

The Basic Framework of Unemployment Insurance

- The federal-state UI system provides state UI benefits to involuntarily unemployed workers. Regular state UI benefits last 26 weeks (in all but two states). They are financed through state UI payroll taxes and paid from state trust fund accounts maintained in the U.S. Treasury.
- Separate federal UI trust funds are supported by a federal UI payroll tax and pay for the entire cost of state and federal UI administration and for federal extended benefits paid through the Emergency Unemployment Compensation program enacted in July and expanded in November 2008.
- Currently, state trust funds total more than \$31 billion overall, and federal trust funds exceed \$35 billion. Both state and federal UI trust funds are legally dedicated solely to the payment of UI benefits and program administration.
- Current federal payroll taxes under the Federal Unemployment Tax Act (FUTA) are imposed only on the first \$7,000 of wages at an effective tax rate of eight-tenths (0.8) percent, or \$56 per covered employee.

Investments in UI Benefits Boost States' Economies

- Unemployment Insurance is referred to as the "first line of defense" in the event of a recession, not just because it is relied upon to provide income support to laid off workers but also because money paid out in UI benefits during recessions significantly boosts and stabilizes the economy. State survey data indicate that nearly all families on UI quickly spend their entire UI check, as opposed to other forms of

stimulus that might be saved rather than spent.¹ A national random sample found that 77% of UI recipients reported that the benefits were very important to their families needs with the bulk of their UI checks going to food and housing.²

- Economists of all persuasions applaud the “countercyclical” nature of the UI program and its documented impact on economic growth. In fact, a major study of five post-WWII recessions found that unemployment benefits contributed \$2.15 in economic growth for every dollar of benefits paid to jobless workers.³ When more jobless workers end up collecting UI and they collect more in benefits, state UI programs will have a bigger role in boosting states’ economies.

States UI Programs Fail to Adequately Support the Unemployed

- The current recession is expected to last at least two years and result in unemployment levels exceeding 8.5 percent. There is an urgent need for a strong safety net to help jobless workers support themselves and their families while they search for new work. Moreover, struggling state economies can greatly benefit from the infusion of cash provided by the UI program when benefits rise.
- However, far too many workers now fall through the cracks of state UI programs. Nationally, only 37 percent of unemployed workers collect UI benefits, and several states pay benefits to fewer than one in four unemployed workers. As a result, absent reforms to strengthen their UI programs, these states will provide minimal protection to laid off workers and reap only limited benefits from the economic boost provided by UI benefit payments.
- Low-wage, part-time and women workers are hit hardest by outdated state eligibility rules, creating a special hardship on those families (many of them recently employed after coming off of welfare) who can least afford to miss out on UI benefits during a recession.
- In today’s economy, with large-scale layoffs in manufacturing and spreading economic risks from global competition, workers are struggling for much longer periods of time to find increasingly scarce jobs and to get training and other help they need to find quality jobs in new fields of employment. With appropriate policies, UI programs can do much more to help workers get the support they need to participate in training and make ends meet during extended periods of unemployment.

While Several State UI Trust Funds Are Prepared for Recession, A Substantial Number Are Not

- Roughly half the states have strong reserves in their UI trust funds that should enable them to withstand the surge in claims occurring throughout the country. These states had more than a year of recession-level benefits still in their trust funds as of September 30, 2008.
- As many as 19 states could have trouble meeting their UI benefit obligations in 2009 or 2010, and some could be forced to take on federal loans to continue paying benefits. NELP is particularly concerned with solvency issues in Michigan, South Carolina and Indiana (who have already taken or applied for loans) and in New York, Ohio, New Jersey, California, Kentucky, Wisconsin, Rhode Island, and Arkansas.⁴ In a longer or deeper than average recession, other states will face challenges.
- While some of these states have been hard hit by joblessness, most state trust fund problems are due to irresponsible financing that failed to build up reserves in good times to pay benefits in response to a

recession. The number of states meeting the recommended pre-recession savings level (a whole year of peak level benefits saved) declined from 28 states in 2000 to 18 states in 2007.⁵

- The automatic mechanisms meant to help states recover from recession level claims are not functioning because UI taxes are only assessed on a small proportion of employer payrolls. On average, employers are free and clear of their obligations to pay UI taxes once each employee has earned \$11,500. This state taxable wage base can be as low as \$7,000, and most states do not index their taxable wage bases to inflation. One recent analysis found that the 14 states with indexed taxable wage bases were five times as well-prepared for the recession as large states that don't use indexing and are facing serious fund problems.
- To address short-term trust fund problems, states can take advantage of loans from the federal government, which are interest free in the first year. The availability of loans gives states time to craft a long-term solvency plan. Most states in solvency trouble today took years to land in their current predicament, and restoring responsible financing will also require a multi-year plan.

A State Agenda to Strengthen UI & Weather the Recession

Responding to the severe challenges due to the current recession, state legislators and governors should consider the following measures that will significantly strengthen the UI safety net, enhance the economic security of laid off workers and provide much-needed economic stimulus to fight state recessions. With state legislative sessions beginning in January, and active debates taking place to respond to the severe hardship of today's recession, the timing could not be better to move aggressively to modernize the state unemployment insurance programs. Model legislation is attached to help implement these proposed reforms (Appendix).

1. Expand Eligibility to Capture More Low-Wage & Part-Time Workers

Because of outdated eligibility rules, most unemployed workers – over 60% in 2007 -- don't collect UI. Restrictive state UI laws create an ever more severe problem for low-wage, part-time and women workers. For example, a U.S. General Accountability Office (GAO) study found that low-wage workers were twice as likely to be laid off as higher wage workers, but only a third as likely to collect UI benefits when they were laid off.⁶ To address shortcomings, states should consider a number of reforms that other states have already put into place.

- Adopt the Alternative Base Period. The "alternative base period" (ABP) is a significant reform to expand eligibility for low-wage workers, new entrants to labor market, and seasonal workers.⁷ It requires states to use the worker's more recent wages to measure UI monetary eligibility (most states don't otherwise count the individual's most recent 3-6 months of wages needed to qualify for UI). Twenty states and the District of Columbia (Connecticut, Georgia, Hawaii, Illinois, Maine, Massachusetts, Michigan, Minnesota, New Hampshire, New Jersey, New Mexico, New York, North Carolina, Ohio, Oklahoma, Rhode Island, Vermont, Virginia, Washington, and Wisconsin), representing about one-half of the nation's UI claims, have already done so. The ABP helps 40 percent of those who would otherwise be monetarily ineligible under the old rules qualify for UI.
- Level the Playing Field for Part-time Workers. More than one in six of all workers are part-time, but in more than half of the states, part-time workers cannot collect UI because states require UI claimants to be able to accept full-time work, even if they meet UI state monetary eligibility requirements through

part-time work. These workers are predominantly women and disproportionately low-income. States should eliminate the restrictions on an individual's part-time work search where it's clear that part-time job opportunities exist.

- Recognize Compelling Domestic Circumstances for Leaving Work. Most states don't permit "personal" reasons to qualify as "good cause" for leaving work, thus denying UI to many women workers in particular. Several states, however, cover "compelling domestic circumstances" as valid reasons for leaving work and collecting UI. These and other more targeted "good cause" provisions protect workers forced to quit work to care for sick children, partners or parents; leaving work due to child care/shift work conflicts; or quitting due to domestic violence. Significantly, these benefits are not "charged" to the employers, meaning that the employer's UI tax rate is not increased when the worker collects UI. When good jobs are even harder to find due to the recession, working families should not be denied UI simply because they are forced to leave work to accommodate urgent family needs.

During the 2001-2004 jobs slump, more than a dozen states took action to make their safety net more responsive to low-wage, women and part-time workers, and there is keen interest in these reforms again as the economic downturn has placed a spotlight on the shortcomings of the unemployment program. Congress has recognized the importance of these key reforms by proposing the Unemployment Insurance Modernization Act, which would deliver \$7 billion of incentive awards to states that enact these key reforms.

2. Boost the Value of UI Benefits & Extend the Weeks of Support

Too many states pay inadequate weekly UI benefit amounts, thus undermining the program's ability to support working families and to invest new resources to help stabilize the economy. To address this fundamental gap in the unemployment program, states should adopt the following reforms:

- Increase and Index the Average Weekly UI Benefit. States should increase their UI benefit levels by replacing a higher percentage of the worker's previous wage and indexing benefits to the state's average weekly wage. Currently, state UI benefits average just \$295 a week, replacing only 34% of the states' average weekly wage. The average weekly benefit ranges from \$414 a week in Hawaii to \$181 in Mississippi. 32 states now also index their unemployment benefits, usually in relation to the state's average wage. In the midst of the decline in the economy, several states have recently raised their benefits. For example, Alaska increased its maximum benefits from \$248 to \$370, and both Louisiana and Mississippi bumped their maximum weekly benefit up by more than \$20 per week earlier this year.
- Eliminate or Suspend the "Waiting Week". Most states -- all but 14 -- require workers who qualify for UI to serve a one-week waiting period before collecting their first UI check, thus eliminating one week of benefits for everyone except those who end up exhausting their 26 weeks of state benefits. Some states have entirely eliminated the waiting week, while others reimburse workers for the one week if they collect UI for longer than several weeks.
- Reduce Offsets Against UI Benefits. Many states offset UI benefits against various other sources of income, including severance pay, IRA rollovers and Social Security retirement benefits. In other words, workers who receive severance or other forms of income see their unemployment check fully or partially reduced. To maximize the income available to laid off workers, and assist the increasing number of workers who are urged to accept layoff packages in a declining economy, all states should revisit these policies and reduce or eliminate selected offsets that deny UI benefits to

laid off workers. Since 2003, 19 states have eliminated or reduced their social security offset as state policy makers have recognized the unfairness of these policies.

- Expand the length of UI benefits. The common understanding of the UI program is that jobless workers qualify for 26 weeks of state unemployment benefits. In fact, only 9 states guarantee 26 weeks of benefits to all workers who qualify for coverage. The other states vary the duration of unemployment benefit—usually by capping total unemployment benefits at a fixed percent of prior earnings. Several states including Georgia, Florida, Arkansas, and Oregon, provide some claimants with less than 10 weeks of benefits, and those earning below average wages are more likely to be short changed. As jobless workers struggle to find work in today’s flagging job market, there is a strong case to be made for providing longer periods of unemployment benefits. For example, New Jersey recently permanently changed the length of state unemployment benefits from 75 percent of the number of credit weeks worked to 100 percent of credit weeks, hence helping a greater share of its unemployed collect 26 weeks of benefits. The most straightforward approach is to provide all workers with 26 weeks of benefits, and this uniform duration approach is used in 9 states.
- Extended Benefits for Workers in Training. During hard economic times, workers are often best advised to seek retraining. However, most workers can’t afford to participate in training while they are unemployed unless they are also provided with income support. Under federal law, workers cannot be denied UI while participating in state-approved training programs. In addition, several states have enacted model programs allowing unemployed workers to collect supplemental UI benefits while in training. New York recently adopted major reforms to its extended benefits for training program, providing workers with the flexibility to seek training to change careers if they can demonstrate that training would help them move from unstable, low wage jobs to more sustainable employment. In total, seven states provided extended benefits for workers in retraining classes, and these states typically provided an additional 26 weeks of benefits in approved cases.
- Adopting Optional Extended Benefit triggers – Currently, workers are counting on temporary extensions of federal benefits to provide extra weeks of benefits for the long-term unemployed. States can act on their own to ensure that benefit extensions are available to back up those provided by federal-funded extensions. Federal law allows for an automatic extension of benefits through the permanent federal extended benefits program (EB) for any states whose unemployment rate tops 6.5%. However, states have to adopt this optional trigger standard in their law to qualify. States that have adopted the trigger already will be able to provide extra weeks of benefits to workers who exhaust the temporary extension of benefits, and are still unable to find workers.

3. Additional Measures of Special Significance During Recessions

- Prevent Abuse of Work Search Requirements. All states require workers to be looking for work while collecting UI and to be willing to accept suitable work. Although often under enforced, federal UI law also imposes special protections related to the kinds of jobs that workers can be made to accept by the state to continue receiving UI. When jobs are scarce and UI state funds are more stressed, there may be more pressure in some states for workers to be forced to accept substandard jobs (e.g., temporary work or lower paying jobs) as a result of the suitable-work requirement. State policy makers should protect against stricter enforcement of the suitable work requirement and enact clarifying legislation where necessary. More generous work search policies

can also be adopted, such as waiving the work search rules when the unemployment rate exceeds significant levels within a state (this provision exists in at least one state, Michigan).

- Explore Work-Sharing (or Short-Time Compensation) Programs. A number of states (Arizona, Arkansas, California, Connecticut, Florida, Iowa, Kansas, Louisiana, Maryland, Massachusetts, Minnesota, Missouri, New York, Oregon, Rhode Island, Texas, Vermont and Washington) operate special UI programs that allow employers faced with the need to layoff workers to instead reduce the hours of the workforce and provide UI benefits to help fill the gap in the missing wages of the workers. These programs differ among the states, but they generally require the employer (and the union, where one exists) to petition the state to operate the program. In some states, including California and New York, the duration of UI benefits in these cases is limited to less than the normal 26 weeks. In addition, while collecting short-time compensation, workers generally need to work four days a week in order to avoid significant wage losses. Short-time compensation programs are not a panacea, but they are a valid way to avoid layoffs in targeted situations.
- Improve Partial Unemployment Benefit Programs. During periods of rising unemployment, instead of being laid off, some workers have their hours reduced and the number of such underemployed workers has skyrocketed to a record 7.3 million Americans in November 2008. All state laws permit workers facing reduced hours of work to draw "partial" or "underemployment" UI benefits while continuing to work part-time. In general, a worker must earn less than his or her weekly UI benefit in a week of less than full-time work to collect partial UI benefits. A major problem with these programs is that the UI benefits are substantially offset against the individual's wages. To address this inequity, states should enact substantial earnings disregards that apply to partial UI benefits. The income disregards now range from the entire weekly benefit amount in Puerto Rico and one-half the weekly benefit amount in Idaho, Illinois and Nebraska, down to one-fifth of the weekly benefit amount in New Hampshire, New Mexico, Ohio and Rhode Island.
- Protect Downsized Workers. Many states reduce or deny unemployment benefits when workers accept early retirements or lump-sum incentive packages during mass layoffs or workplace closings. For example, before mass layoffs many employers offer workers lump-sum packages in exchange for leaving work and signing a release/waiver. If enough workers in the group do not accept the incentives, involuntary layoffs without the lump-sum payments follow. Several states hold that these separations are "voluntary" on the part of the workers accepting the lump sums, while others offset UI benefits against the lump sum, effectively denying UI benefits. Given the overall circumstances, these separations are hardly "voluntary" and should not be disqualifying. When lump sum payments represent a cash incentive to give up employees' fringe benefits, seniority and severance pay, or payments are conditioned upon a release of other potential legal claims, they should not be considered wage replacements that properly offset UI benefits. In other words, these payments are consideration paid in return for what the jobless workers are giving up, not payments to replace lost wages. In addition, state laws prohibit the waiver of UI benefits, so the "agreements" signed by employees should not be treated as giving up rights to UI. State laws should preserve the income of laid off workers, rather than penalizing these workers by imposing disqualifications and offsets in these situations.
- Bolster State Training in Partnership with the Unemployment Program: In response to sharp federal workforce funding cuts in recent years, nearly half the states now raise money in partnership with their state unemployment programs. These states typically add a small incremental assessment on employer tax bills and then direct those resources to a targeted

training program. Funds are typically used to help dislocated workers access retraining they need to return to work or to help incumbent and/or low-skilled workers upgrade their skills to become more competitive. In several states, like Minnesota and New Jersey, state training dollars now dwarfs federal workforce investment act grants.⁸

To learn more about these policies, please contact the National Employment Law Project
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¹ State of Washington Employment Security Department "Claimant Expenditure Survey, Fiscal Year 2007," January 2008, available at <http://www.esd.wa.gov/newsandinformation/media/uipublishedreports/claimant-expenditure-survey-2007.pdf>

² Hart Research Associates, "Unemployed In America: Job Market, Prospects for Employment, and Impact of Unemployment on Families and the Unemployed," commissioned by the National Employment Law Project, December 2008. Available at <http://www.nelp.org/page/-/UI/show8860.pdf>

³ Lawrence Chimerine, et al., *Unemployment Insurance as an Economic Stabilizer: Evidence of Effectiveness Over Three Decades* (1999).

⁴ National Employment Law Project, "Unemployment Insurance Financing: State Trust Funds In Recession as Of September 30, 2008." (November 2008) Available at <http://www.nelp.org/page/-/UI/Trust%20Fund%20Solvency%20Update%202008-Final.pdf>

⁵ National Employment Law Project, "Unemployment Insurance Financing: Examining State Trust Funds Facing Recession," (May 2008).

⁶ U.S. General Accountability Office, "Unemployment Insurance: Receipt of Benefits Has Declined, with Continued Disparities for Low-Wage and Part-Time Workers," GAO-07-1243T, September 19, 2007.

⁷ National Employment Law Project and the Center for Economic and Policy Research, "Clearing the Path to Unemployment Insurance for Low Wage Workers" (September 2005).

⁸ National Employment Law Project, "Expanding State Education and Training By Partnering with the Unemployment Insurance Program" (September 2008).