Statement
Of
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I am Douglas J. Holmes, President of the National Foundation for Unemployment Compensation and Workers' Compensation, a research foundation that annually publishes comparisons of state unemployment compensation laws and hosts the National Unemployment Insurance Issues conference.

I also serve as President of UWC Strategic Services on Unemployment & Workers' Compensation (UWC), the national membership organization serving as the voice of business specifically with respect to unemployment insurance. UWC and its predecessor organization have served the business community in analysis of unemployment insurance policy since 1933. UWC members include a broad base of national and state business organizations as well as individual employers with specific interest in unemployment insurance.

I spent most of my professional career as UI Director, Legal Counsel and/or Deputy Administrator for workforce programs in Ohio and supervised or directly served as the Secretary of the Unemployment Compensation Advisory Council in Ohio over a period of 21 years from 1984 through 2005. During that period the council recommended over 20 UI related bills for enactment by the Ohio General Assembly. All of them were enacted with very large bi-partisan votes of support.

The Employment Security System is an employer financed insurance system designed to provide temporary, partial wage replacement for individuals in employment who have become unemployed through no fault of their own in connection with work, and as a condition of being paid unemployment compensation the individual must be able to work, available to work and actively seeking work.

Pennsylvania is one of a number of states that developed large deficits with increased claims during and after the recession of 2008 -2009. The positive balance in the state unemployment benefit account stood at $1.7 billion as of the end of the second quarter of 2008 yet was quickly depleted, becoming a deficit one year later with a loan from US DOL of $528 million.

By the second quarter of 2010 the federal loan had grown to $3.0 billion, and by 2011 it had grown to $3.7 billion. Pennsylvania took action to enact solvency legislation and approve bonds to pay off the outstanding balance to avoid FUTA tax increases that would be automatically imposed and to seek long term balance between benefit payout and tax revenue. The immediate measures have had a positive effect on the solvency of the state UI trust fund.

As of the end of first calendar quarter of 2015 the state unemployment trust fund had a balance of $171 million. Tax revenue being received on an annual basis has increased to $3.1 billion while benefit payout is about $2.3 billion.

Although the solvency picture has improved, the state is still a long way from being solvent so as to avoid having to borrow when the next recession occurs. It is premature at this point to take legislative action that increases benefit payout.

The 1.0 Average High Cost Model (AHCM) guideline recommended by the US Department of Labor is a measure that is recognized as being actuarially prudent, and serves as a standard goal for solvency as a condition of states being eligible for interest free short term cash flow loans from US DOL.

Key comparisons with surrounding states show that Pennsylvania provides unemployment compensation amounts that are still relatively high and employer tax and bond debt service assessments that are also high compared to other states. Although the state shows a positive balance in its unemployment trust fund account, there remains a significant bonded indebtedness.

Average Weekly Benefit Amount for the four quarters ending the first quarter of 2015

PA	366
OH	331
NJ	406
MD	325
NY	310
WV	283
DE	248

UI Tax as Percent of Total Wages and Related Debt Burden

PA	1.28 plus Bond debt service
OH	0.62 plus FUTA deficit increase tax
NJ	1.28
MD	0.55
NY	0.78 (recently paid off UI Loans to eliminate FUTA increase for 2015)
WV	0.99
DE	0.75

UI Trust Fund Balance

PA	171m with outstanding Bond to be repaid
OH	138m with outstanding FUA loan balance to be repaid
NJ	256m
MD	736m
NY	8m
WV	65m
DE	14m

The outstanding burden in Pennsylvania (combined with Bond debt) is higher than all of the states surrounding it and among the highest in the country.

Qualifying Formula for Unemployment Compensation

The unemployment compensation system requires that there be some meaningful workforce attachment as a condition of individuals establishing a period of benefit eligibility. The most common formula used by states is a high quarter formula that requires a specified amount of wages in the individual's four quarter base period and an amount in the quarter within the base period for which the highest amount was paid. Many states also use monetary requirements tied to base period wages along with a requirement that there must have been wages paid to the individual in at least two or more quarters.

Forty-Six states require that wages be paid in more than one quarter as a condition of an individual qualifying for benefit rights, and most specify dollar amounts per quarter or require that the amount outside the high quarter be at least one-half of the high quarter wages. Nineteen states use the one and one-half high quarter requirement that effectively requires that an individual have been paid at least 50% of his or her wages in quarters other than the high quarter.

Trust Fund Solvency Observations

Projections of trust fund balance that assume continued low benefit payout all the way through 2019 are unrealistic given the history of economic expansions and contractions. To be prepared, the state should run scenarios assuming a recession in 2017 and 2018. In states in which minimum wage increases are expected, projections should factor in increases in the number of individuals qualifying monetarily and increases in the weekly benefit amounts that are tied to wages.

Projections should use actual samples of benefit claims and the insured unemployment rate (IUR) in addition to the total unemployment rate (TUR). The TUR is not as accurate in projecting benefit claims costs because it assumes a relationship between the TUR and IUR that changes during a recession as a higher percentage of individuals are laid off and claim benefits. The survey sample used for the monthly TUR is very small and unreliable statistically, and the three month average TUR takes too long to determine while the trust fund is being depleted with claims increases.

States should have a specific solvency target designed to assure that reserves are adequate to pay benefits in a reasonably foreseeable recession and to trigger timely cuts in benefits and/or tax increases.

If the Pennsylvania fund is truly solvent due in large measure to the bonds and employers paying the debt service, why not cut taxes to spur job creation instead of increasing benefits to a group that is cyclically unemployed?

Groups of claimants who are cyclically unemployed impose larger benefit costs on an annual basis than others filing applications, and often are employed by employers who are more likely to be max rated employers (i.e. their contribution rates do not increase with increased benefit charges because they are already paying the maximum rate). Because the UI trust fund is employer financed, increased benefit charges associated with claims against maximum rated employers shifts costs to other employers in the system. Because Pennsylvania is one of only three states that have employee contribution provisions, these benefit payments also increase the risk that employee contributions may need to be increased over time.

Learn from experience. The 2008 recession was not expected by forecasters. In a two year period of time from 2008 to 2010 there was a swing in trust fund balance of more than $5 billion. Planning should include a review of less favorable assumptions about the performance of the economy and a plan to address them in a timely way.

The Average High Cost Multiple (AHCM) is one measure of the amount needed in the trust fund to avoid borrowing during an average size recession based on historical data. Many states do not have a balance that meets the AHCM but they put in place benefit cuts and tax measures to respond immediately to the imbalance. The state can certainly factor in cash flow in its projection. In the 2008 recession the large increases in claims came after the July 1st computation date for taxes for 2009 so that taxes did not spike in many states until 2010 but benefit pay out increased dramatically.

Conclusion

It is premature to enact legislation that has the effect of increasing benefit pay out from the Pennsylvania unemployment trust fund. The requirement that an individual have at least 49.5% of wages in base period quarters other than the high quarter is not unusual among states.

Revisions of solvency measures as the health of the trust fund improves should recognize the long term impact on the trust fund and the burden on individual employers and employees.

All states should learn from the experience of the 2008-2009 recession and earlier recessions that the health of the trust fund can deteriorate quickly as benefit charges increase dramatically while tax increases respond slowly over a period of years. Careful oversight, early recognition of economic trends, and leadership to make timely changes in benefits and/or tax rates is critical to avoiding large deficits and unintended consequences for employers and claimants.