VERMONT
DEPARTMENT OF LABOR

Memorandum

To: The Honorable Phil Scott, Governor

Chair, Senate Economic Development, Housing & General Affairs

Chair, Senate Finance

Representative Bill Botzow, Chair, House Commerce & Economic Development

Representative Janet Ancel, Chair, House Ways and Means

CC:

From: Anne M. Noonan, Commissioner, Vermont Department of Labor

Date: January 4, 2017

Re: UNEMPLOYMENT INSURANCE TRUST FUND REPORT

INTRODUCTION

In partnership with the U.S. Department of Labor's Employment and Training Administration (ETA), the Vermont Department of Labor (VDOL or Department) maintains a statistical model used for forecasting Vermont's Unemployment Insurance (UI) Trust Fund (TF) net[1] balance. This analytical tool is effective in long-run assessments of the overall flow of monies into and out of the UITF. It is also useful in determining the incremental impact of proposed policy changes.

This report and accompanying analysis of the UITF is completed in fulfillment of state law. "On or before January 31 of each year, the commissioner (of labor) shall submit to the governor and the chairs of the senate committee on economic development, housing and general affairs and on finance and the house committees on commerce and economic development and on ways and means a report covering the administration and operation of this chapter during the preceding calendar year. The report shall include a balance sheet of the moneys in the fund and data as to probable reserve requirements based upon accepted actuarial principles, with respect to business activity, and other relevant factors for the longest available period." 21 V.S.A. § 1309.

[1] The ETA UITF model currently functions as a 'net' concept in that the individual UI accounts (loan account, cash account, etc.) are rolled up into a net concept. Out of model analysis is necessary to decipher model results.

SUMMARY OF RECENT UI REFORM

The laws surrounding UI were overhauled in the 2010 legislative session due to Vermont's diminishing, and ultimately negative, UITF balance. The foundation of the reform's efforts was to balance the impacts to employers and UI claimants. The largest impact to employers was the increase in the employers' taxable wage base. The taxable wage base was increased from $8,000 to $10,000 in 2010; to $13,000 in 2011; and to $16,000 in 2012. For this measure, the General Assembly created three triggers that tied future adjustments of the taxable wage base to economic factors. The first provides for the taxable wage base to index upward annually by the same percentage as the annual average wage once the UITF had a balance greater than zero and all Title XII loans were repaid.[2] Indexing of the taxable wage base commenced January 1, 2015 with an increase in the taxable wage base from $16,000 to $16,400. At the start of 2016, the taxable wage base was indexed to $16,800 and then indexed again on January 1, 2017 to $17,300. The second trigger is effective upon return to Tax Rate Schedule III at which time the taxable wage base will drop by $2,000. The third trigger is effective upon return to Tax Rate Schedule I at which time the taxable wage base will drop by an additional $2,000. No indexing occurs in the year in which the second and third triggers are met.

Additional 2010 Reforms Relating to Employers:

- Increased late filing penalties from $35 to $100, and provided that employer accounts could not be relieved when untimely or inaccurate reporting led to an overpayment of benefits.
- Establishment of a misclassification penalty of up to $5,000 for each improperly classified worker. In addition, provided that an employer found to have misclassified workers would also be prohibited from contracting with the State for up to three years.
- Shortened time period for timely reporting of new hire information from 20 to 10 days.

The following is a list of changes that impacted UI Claimants:

- Modification to the maximum benefit amount payable in a benefit year. The new formula established that a claimant would be eligible for an amount equal to 26 weeks times their weekly benefit amount or 46% of the base period wages, whichever is less.
- Capped maximum benefit amount (to 23 weeks) for a worker found to have separated from his or her last employer due to misconduct.
- Exclusion of usable wages for claimants found to have caused their own separation from employment due to gross misconduct (as determined by the Department).
- Capped the weekly benefit amount (WBA) at $425 and tied the annual adjustment of the maximum weekly benefit amount (MWBA) to economic factors.

[2] Vermont had borrowed $77.7 million from the U.S. Department of Labor between February 2010 and April 2011. The VDOL stopped all borrowing by April 2011, and paid back the federal loan by July 1, 2013, 18 months ahead of the earliest projected pay-off date.

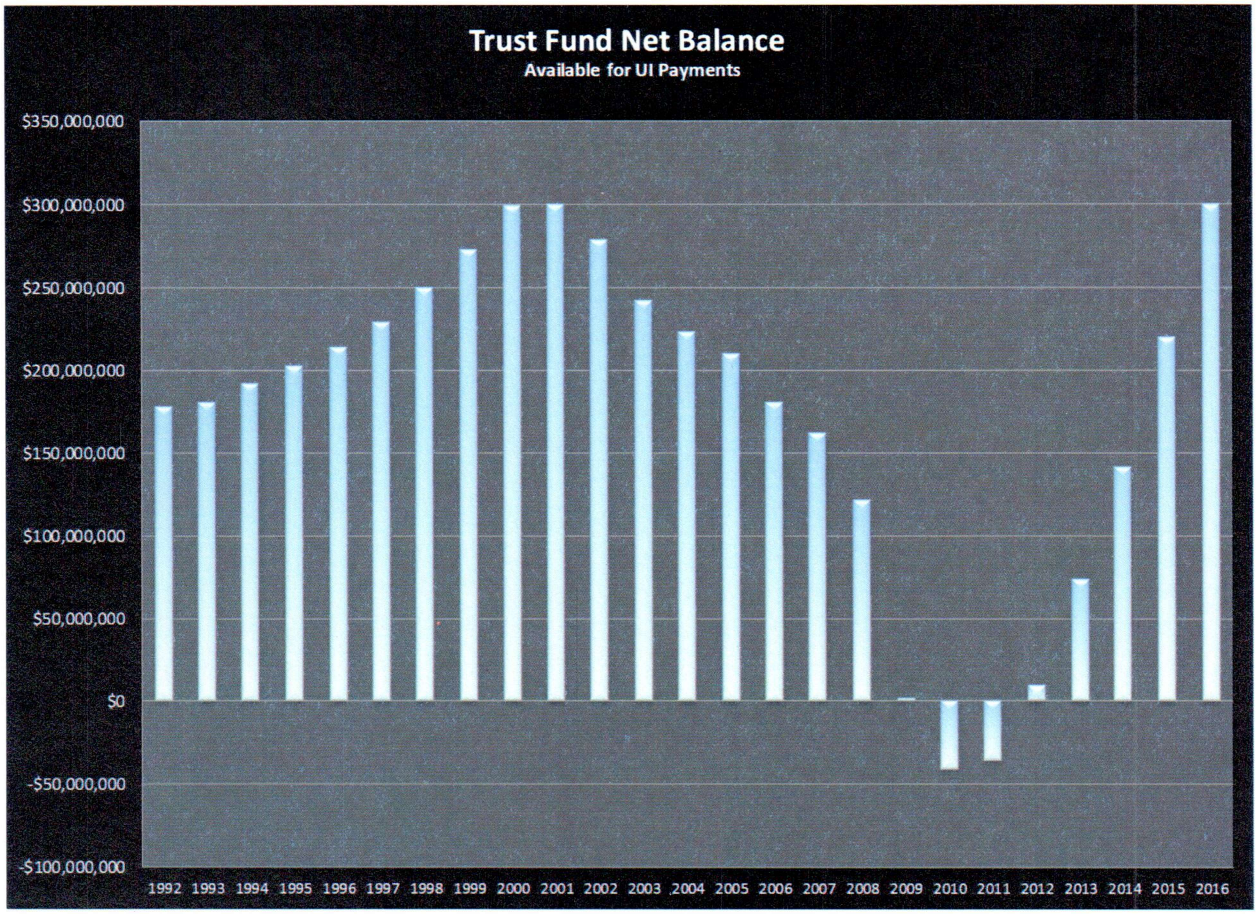
  - When the UITF balance is greater than zero and all Title XII loans repaid, the MWBA will be adjusted by a percentage equal to the percentage change during the preceding calendar year in the statewide average weekly wage. As projected, indexing commenced in July 2014 with the increase in MWBA from $425 to $436 per week. Currently, the MWBA is $458 per week.
  - Effective the first Sunday in July, upon return to Tax Rate Schedule III, the MWBA for all new initial claims will be equal to 57% of the statewide annual average weekly wage, returning the MWBA to its position prior to the reform relative to the average wage.
- Increase in the maximum number of weeks that can be disqualified when it has been determined a claimant was discharged.
- Established that severance pay shall always be considered disqualifying.
- Implemented a one-week waiting period with an effective date of July 1, 2012. This waiting period does not change the WBA a claimant will receive, but does delay the payment of their first week of benefits. The one-week waiting period will sunset July 1, 2017.

In addition to these measures, the Vermont Commissioner of Labor has also established a work search requirement for individuals with a return-to-work date greater than 10 weeks. As a result of these changes, both employers and UI claimants are sharing in Vermont's unemployment insurance reform. While these represent the most substantial changes to UI laws, there have been more recent adjustments, including Disregarded Earnings.

During the 2014 legislative session the Disregarded Earnings was increased from 30% to 50% of an individual's weekly wage. This provision is designed to encourage UI claimants to accept less than-full-time jobs while remaining eligible for at least a portion of their unemployment benefits. A Self-Employment Assistance (SEA) program was also enacted during this session. The SEA program is designed to encourage and enable unemployed workers to create their own jobs by starting their own small businesses.

BACKGROUND

From the period of 2001 to 2010, Vermont's UITF's annual debits exceeded their credits. As depicted in graph below, the State went from having a positive UITF balance in 2001 of $300.4 million to a negative balance of -$40.6 million by 2010. This required the State to borrow money from the U.S. Federal Government and cover their debts through a Title XII loan. The loan amount increased to $77.7 million in 2011 due to shortages of cash in the first quarter of that year. Due to the changes in the State's UI laws and improved economic conditions, 2011 was net positive in that more cash was collected in contributions than was paid out in the form of UI benefits. This was the first time since 2001 that the UITF has experienced a net positive contribution to benefit ratio. This positive accrual trend established in 2011 has continued annually to the current year. The ending UITF net balance on December 31, 2016 is estimated to be $299.9 million (see below).



As a means of limiting future interest owed to the federal government, the Vermont Commissioner of Labor authorized the partial repayment of the Title XII loan. Effective July 20th, 2012, a payment of $20M was applied against the outstanding Title XII loan balance reducing the amount owed to $57.7M. The remaining balance on the federal Title XII loan was repaid in full on July 1, 2013. The complete repayment of the loan ceased the accrual of additional loan interest and reinstated the full Federal Unemployment Tax Act (FUTA) tax credit for Vermont employers. Previously for calendar year 2012, due to the duration of the outstanding federal loan, Vermont employers experienced a reduction in the FUTA tax credit by 0.3%. This equated to an additional charge to employers in the form of higher FUTA taxes collected. Had the loan not been repaid in 2013, employers would have experienced an additional 0.3% FUTA tax credit reduction for a total tax credit reduction of 0.6% due in January 2014.

<u>DECEMBER 2016 MODEL FORECAST</u>

The level of contributions is governed by the tax rate schedule in effect for Vermont employers. The tax rate schedule is determined annually in July via a calculation considering both the historical utilization of the fund and the current fund balance. For the past several years, employers have been paying at the highest of the five tax rate schedules – level five or "V". In July 2016, the calculation fell just short of the threshold necessary to migrate to tax rate schedule IV. It is anticipated in both the baseline forecast and the 'theoretical recession' forecast that the balance in the UITF will be sufficient to move down to tax rate schedule IV in July 2017. All else equal, this will mean a reduction in the UI tax rate Vermont employers pay.

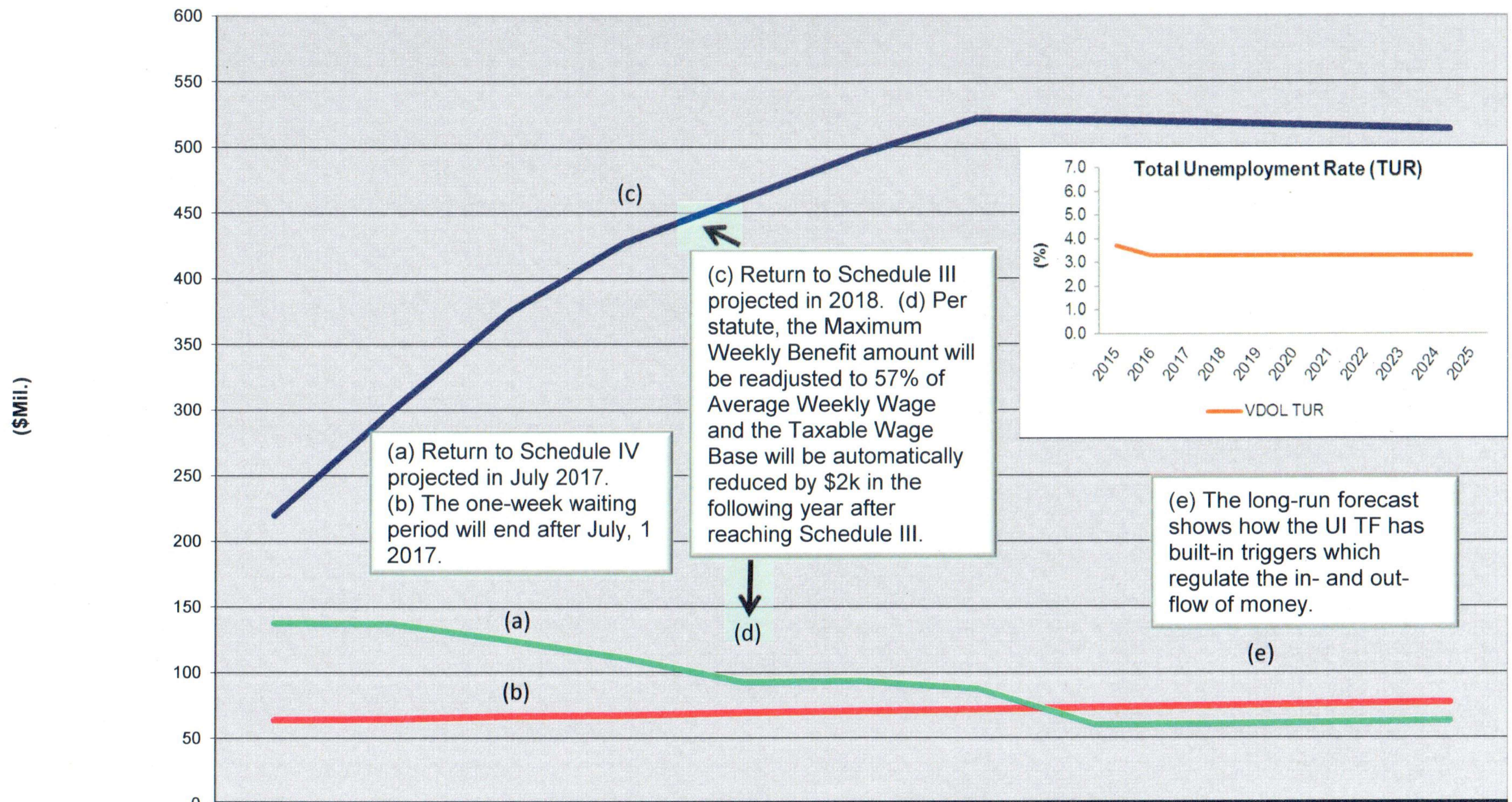
Beyond anticipating the move to tax rate schedule IV in 2017 which seems definite, there is less clarity about future tax rate schedule migrations. Even though both the baseline forecast and the 'theoretical recession' forecast show a migration to tax rate schedule III in July 2018, this is not certain. As has been the practice, an alternate 'theoretical recession' as been modeled to provide insight on how the UITF will respond to a potential economic downturn. The theoretical recession is based on historical data and forecasted to occur two years in the future. The next recession could begin at any time – either before or after this arbitrary two-year parameter. Should an economic downturn begin sooner than 2019 as modeled, it is possible the migration to tax rate schedule III could be delayed. Based on current economic conditions, the balance will have to meet or exceed $340M to trigger migration to tax rate schedule III. It does seem likely this will occur in 2017 but it is not guaranteed.

<u>FORECAST RISKS</u>

Changes to federal or state UI laws: The attached forecast is based on current law – both federal and state. Should these laws change, this forecast will have to be reevaluated. It is important to note that there are natural dampening agents built into Vermont's UI laws which will automatically throttle back employer contributions when the UITF has a significant positive balance.

National and international economic uncertainty: The U.S. economy seems to have stabilized and is remaining in a period of economic expansion – albeit a slower rate of growth than historical periods of expansion post-recession. Yet in this modern age of globalization, it is difficult to determine the U.S.'s exposure to international economic pressures around the globe. In addition, unforeseen volatility in energy prices and/or supply could create a ripple sufficient to derail the U.S. economic recovery. Threats of international entanglements also remain areas of concern for the forecast.

Vermont Unemployment Insurance Trust Fund Baseline Forecast - December 2016



	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Trust fund Net Balance	219.9	299.9	375.0	427.6	461.1	494.8	522.1	520.8	518.7	516.3	513.7
Benefis	64.1	64.7	66.8	67.5	69.4	70.7	72.0	73.3	74.7	76.0	77.3
Contrilutions	137.9	137.3	124.7	111.3	93.1	94.0	88.1	60.6	61.1	62.3	63.5

NOTES:
- The Trust fund Net Balance is a theoretical total of cash offset by any loan amount as applicable; Loan repaid in 2013.

SOURCE: VJOL Benefit Finance Model, Dec. 2016, unless otherwise noted.

Vermont Unemployment Insurance (UI) Trust Fund Baseline Forecast - December 2016

		Benefits				Contributions	
Year ^	Trust Fund Net Balance ($Mil.)	Regular Benefits ($Mil.)	Extended Benefits ($Mil.)	Total Benefits ($Mil.)	Max Weekly Benefit**	Total Contributions ($Mil.)	Taxable Wage Base
2015	219.9	64.1	0.0	64.1	446	137.9	16,400
2016	299.9	64.7	0.0	64.7	458	137.3	16,800
2017	375.0	66.8	0.0	66.8	468	124.7	17,300
2018	427.6	67.5	0.0	67.5	513	111.3	17,700
2019	461.1	69.4	0.0	69.4	524	93.1	15,700
2020	494.8	70.7	0.0	70.7	536	94.0	16,000
2021	522.1	72.0	0.0	72.0	548	88.1	16,400
2022	520.8	73.3	0.0	73.3	560	60.6	14,400
2023	518.7	74.7	0.0	74.7	572	61.1	14,700
2024	516.3	76.0	0.0	76.0	585	62.3	15,000
2025	513.7	77.3	0.0	77.3	597	63.5	15,300

Year ^	Total Unemployment Rate*	Total Wages ($Bil.)	Taxable Wages ($Bil.)	Wage Growth*	Labor Force Growth*	Tax Rate Schedule**
2015	3.7	9.1	3.6	2.8%	-0.01%	5
2016	3.3	9.1	3.6	3.0%	0.10%	5
2017	3.3	9.2	3.6	2.2%	-0.15%	4
2018	3.3	9.4	3.7	2.2%	-0.15%	3
2019	3.3	9.6	3.4	2.2%	-0.15%	3
2020	3.3	9.8	3.5	2.2%	-0.15%	3
2021	3.3	10.0	3.5	2.2%	-0.15%	1
2022	3.3	10.2	3.2	2.2%	-0.15%	1
2023	3.3	10.4	3.3	2.2%	-0.15%	1
2024	3.3	10.6	3.3	2.2%	-0.15%	1
2025	3.3	10.9	3.4	2.2%	-0.15%	1

Year ^	Interest Rate %‡	Interest Earned ($Mil.)	End of Year Loan Amount ($Mil.)*	Interest Payable September 30 ($Mil.)*	FUTA Credit Reduction %	FUTA Credit Reduction Payment Jan 1 ($Mil.)
2015	3.38	4.4	0.0	0.0	0.0	0.0
2016	2.23	6.0	0.0	0.0	0.0	0.0
2017	2.23	7.5	0.0	0.0	0.0	0.0
2018	2.23	8.8	0.0	0.0	0.0	0.0
2019	2.23	9.8	0.0	0.0	0.0	0.0
2020	2.23	10.5	0.0	0.0	0.0	0.0
2021	2.23	11.2	0.0	0.0	0.0	0.0
2022	2.23	11.5	0.0	0.0	0.0	0.0
2023	2.23	11.4	0.0	0.0	0.0	0.0
2024	2.23	11.4	0.0	0.0	0.0	0.0
2025	2.23	11.3	0.0	0.0	0.0	0.0
Totals				**0.0**		**0.0**

NOTES & SOURCES:
* VDOL E&LMI Projections.
^ #s are as of end of year; 2015 are actual data; 2016 are estimates.
‡ Based on Fiscal Years; The interest rate is a forecast provided by USDOL.
** Maximum Weekly Benefit and Tax Rate Schedule change on July 1.

SOURCE: VDOL Benefit Finance Model, Dec. 2016, unless otherwise noted.

Forecast Parameters Extracted From Bill S. 290 (ACT 0124)

Title: An Act Relating to Restoring Fund Adequacy to the UI Trust Fund

Taxable Wage Base (TWB)
Beginning January 1, 2012, the TWB will remain at $16,000 until the Trust Fund has a positive balance on June 1 (with no outstanding loan amount), at which point the TWB will index upward annually by overall wage growth as determined by the QCEW program beginning January 1 of the following year and thereafter. Based on the July 1, 2013 date of repayment for the Title XII loan, the TWB began indexing on January 1, 2015 and will continue annually thereafter.

When the unemployment contribution rate schedule is reduced to Schedule III, the TWB will be reduced by $2,000 on January 1 of the following year and will index upward annually by overall wage growth thereafter. When reduced to Schedule I, the TWB will be reduced again by $2,000 on January 1 of the following year and will continue to index thereafter. The first downward adjustment is forecasted to occur in 2019.

Maximum Weekly Benefit (MWB)
The MWB will remain frozen at $425 until the Trust Fund has a positive balance as of December 31 of any given year, at which point the MWB will index upward annually by overall wage growth as determined by the QCEW program beginning the first day of the first calendar week of July of the following year and thereafter. Based on the July 1, 2013 retirement of the Title XII loan, the MWB began indexing in 2014 and will continue annually thereafter.

When the unemployment contribution rate schedule is reduced to Schedule III, the MWB will be adjusted on the first day of the first calendar week in July to an amount equal to 57% of the state annual average weekly wage. An adjustment as previously described is projected to occur in 2018 based on this current forecast.

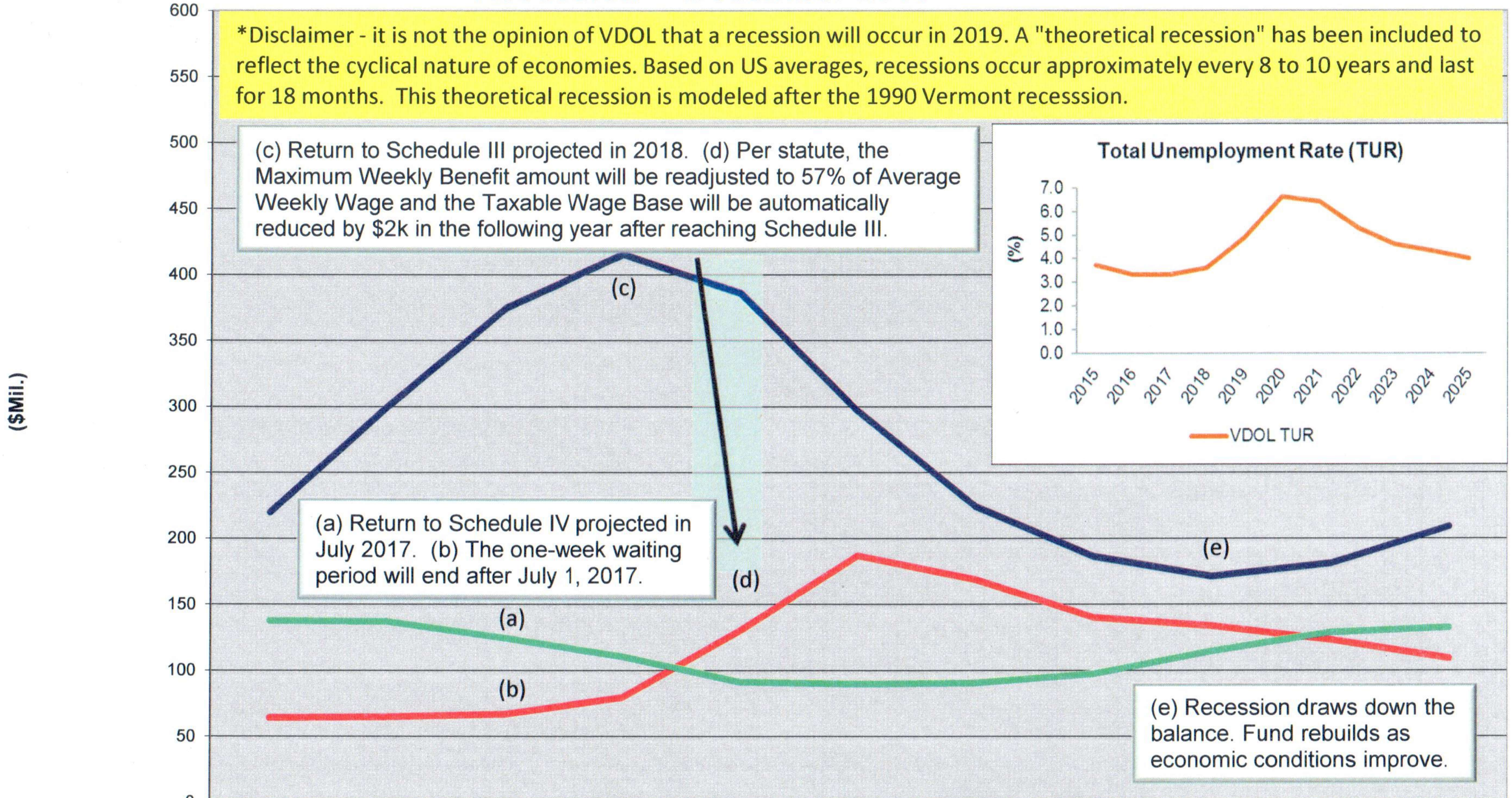
Disregarded Part-time Earnings
For claims established on or after July 1, 2014, 50% of weekly earnings will be disregarded.

Computation of Benefits
For claims established on or after July 1, 2011, the maximum benefits paid during a benefit year will not exceed the lesser of 26 times the claimant's weekly benefit or 46% of the total wages paid to the claimant during the base period.

One Week Waiting Period
For claims established on or after July 1, 2012, a one week waiting period will have to be served before any benefit payment is allowed. The required waiting period will end on July 1, 2017. Claimants are still eligible to receive the full 26 weeks of benefits, just delayed by one week.

Misconduct
For claims established on or after July 1, 2011, findings of simple misconduct will result in a cap of 23 weeks of benefits.

\ermont Unemployment Insurance Trust Fund Forecast with Theoretical Recession* - December 2016



	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Trust Fund NetBalance	219.9	299.9	375.0	415.5	385.9	296.6	224.4	186.5	171.5	181.4	209.2
Benefits	64.1	64.7	66.8	79.3	130.0	186.9	168.9	140.2	133.9	123.2	109.3
Contributions	137.9	137.3	124.7	111.0	91.7	90.2	91.1	98.0	115.1	129.3	132.9

NOTES:
- The Trust Fund Ne Balance is a theoretical total of cash offset by any loan amount as applicable; Loan repaid in 2013.

SOURCE: VDOL Beiefit Finance Model, Dec. 2016, unless otherwise noted.

Vermont Unemployment Insurance (UI) Trust Fund Recession Forecast - December 2016

		Benefits				Contributions	
Year ^	Tust Fund Net Blance ($Mil.)	Regular Benefits ($Mil.)	Extended Benefits ($Mil.)	Total Benefits ($Mil.)	Max Weekly Benefit**	Total Contributions ($Mil.)	Taxable Wage Base
2015	219.9	64.1	0.0	64.1	446	137.9	16,400
2016	299.9	64.7	0.0	64.7	458	137.3	16,800
2017	375.0	66.8	0.0	66.8	468	124.7	17,300
2018	415.5	79.3	0.0	79.3	513	111.0	17,700
2019	385.9	130.0	0.0	130.0	524	91.7	15,700
2020	296.6	179.7	7.2	186.9	530	90.2	15,900
2021	224.4	168.9	0.0	168.9	536	91.1	16,100
2022	186.5	140.2	0.0	140.2	544	98.0	16,300
2023	171.5	133.9	0.0	133.9	556	115.1	16,600
2024	181.4	123.2	0.0	123.2	568	129.3	16,900
2025	209.2	109.3	0.0	109.3	581	132.9	17,300

Year ^	Total Uiemployment Rate*	Total Wages ($Bil.)	Taxable Wages ($Bil.)	Wage Growth*	Labor Force Growth*	Tax Rate Schedule**
2015	3.7	9.1	3.6	2.8%	-0.01%	5
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2017	3.3	9.2	3.6	2.2%	-0.15%	4
2018	3.6	9.4	3.7	2.2%	-0.15%	3
2019	4.9	9.5	3.3	2.2%	-0.15%	3
2020	6.6	9.5	3.3	1.1%	-0.15%	3
2021	6.4	9.6	3.4	1.1%	-0.15%	3
2022	5.3	9.8	3.4	1.5%	-0.15%	4
2023	4.6	10.0	3.5	2.2%	-0.15%	5
2024	4.3	10.2	3.6	2.2%	-0.15%	5
2025	4.0	10.5	3.7	2.2%	-0.15%	5

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2018	2.23	8.7	0.0	0.0	0.0	0.0
2019	2.23	8.8	0.0	0.0	0.0	0.0
2020	2.23	7.3	0.0	0.0	0.0	0.0
2021	2.23	5.6	0.0	0.0	0.0	0.0
2022	2.23	4.4	0.0	0.0	0.0	0.0
2023	2.23	3.8	0.0	0.0	0.0	0.0
2024	2.23	3.7	0.0	0.0	0.0	0.0
2025	2.23	4.2	0.0	0.0	0.0	0.0
Totals				**0.0**		**0.0**

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