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# DEPARTMENT OF LABOR AND EMPLOYMENT

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August 29, 2014

Representative Crisanta Duran, Chair
Joint Budget Committee

Senator Lois Tochtrop, Chair
Senate Committee on Business, Labor and Technology

Representative Angela Williams, Chair
House Committee on Labor, Economic and Workforce Development

Dear Senator Tochtrop and Representatives Duran and Williams:

Pursuant to the reporting requirement contained in HB 11-1288 (8-72-102(3)(b)), I am pleased to transmit this annual report on the status of the Unemployment Compensation Fund (UCF) (also referred to as the Unemployment Insurance Trust Fund). We will also provide a copy of this report to Legislative Council staff and Joint Budget Committee staff for their records.

Thank you again for your continued support and partnership in our efforts over the past several years to stabilize and strengthen the Unemployment Compensation Fund. Please feel free to contact me with any questions, suggestions or concerns about this report or any other matters you would like us to address.

Sincerely,

Ellen Golombek
Executive Director

2014 Colorado Unemployment Insurance Trust Fund Summary Report

The financing structure of the Colorado Unemployment Insurance Trust Fund (UITF) was modified in HB11-1288. The legislation requires that the Colorado Department of Labor and Employment (CDLE) issue a report on the fund's financial condition to several committees of the Colorado General Assembly by August 31 of each year beginning 2012.

This report provides a brief overview of recent UITF developments including the present financial condition of the UITF; the status of the outstanding unemployment compensation bonds; the fund outlook under conditions of moderate economic growth; and efforts the CDLE has taken to reduce improper payments of unemployment benefit made from the UITF.

**Calendar Year 2013 Fund Status.** Fund reserves, which stood at $700 million as of June 2008, were quickly depleted by the sharp, unprecedented rise in job losses experienced between mid-2008 and early 2010.[1] The fund regained solvency in 2012 due to the issuance of $630 million in Colorado unemployment bonds in June 2012. By December 31, 2013, reserves held in the UITF totaled $526.5 million, an improvement of $21.3 million from twelve months earlier when the fund balance stood at $505.2 million.

Employer premiums paid into the UITF totaled $684 million during 2013, down from $829.1 million the prior year. The decrease in employer contributions in 2013 stemmed partly from fewer job layoffs by Colorado businesses which shifted many employers to lower premium rates.[2] Interest earnings on fund reserves, which totaled $7.2 million in 2012, nearly doubled to $14 million in 2013.

Regular unemployment insurance benefit payments fell $43.4 million to $551.5 million during 2013. Although still high by historical standards, annual benefit payments last year declined to their lowest level since 2008. Payments from the UITF, which had averaged about $330 million each year between 2006 and 2008, had climbed to an annual average of $883 million between 2009 and 2011.[3]

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[1] The number of seasonally adjusted nonfarm jobs fell 155,000 or 6.5 percent between the May 2008 peak and the January 2010 bottom. By 2013, however, annual nonfarm employment growth had rebounded to 3.1 percent.

[2] Fund revenues are largely a function of employer premium rates, the fund balance, the rate of employment growth, and the maximum taxable wage base. Individual employer premium rates are determined, in part, by the amount of benefits charged to each employer. Job cuts by Colorado firms have shrunk with the continued improvement in the State's economy thus reducing premium rates for many businesses. The reduction in premium rates offset some of the revenue gains that would otherwise have stemmed from the robust employment gains seen last year. In addition, the solvency surcharge was turned off beginning 2013 and a new premium rate schedule implemented.

[3] In addition to regular state unemployment benefits, since 2008 $3.8 billion was paid to Colorado claimants under the extended unemployment compensation (EUC) and state extended benefits (SEB) programs. Both EUC and SEB were paid with federal dollars and therefore had no direct financial impact upon Colorado's UITF.

**Colorado Unemployment Compensation Bonds.** Several states have issued unemployment compensation bonds in recent years as a way of eliminating the federal debt resulting from having had to borrow from the Federal Unemployment Account in order to meet benefit payments. The Colorado unemployment bonds differ from those issued by other states in that the bond proceeds and principal repayments flow through the UITF. Structuring the bonds in this way allowed the bond principal repayments, which are made by Colorado employers, to be credited to their employer experience rate accounts and thus lower their premium rates below what they otherwise would have been.

The bonds, which totaled $630 million, have a five-year term and require fixed annual principal repayments of $125 million to be made each May through 2017—the Department made the second annual principal payment May 15, 2014. The revenue for the principal repayments comes from Colorado employers who are billed a bond principal repayment surcharge as part of their annual unemployment insurance premiums. This bond principal surcharge will vary slightly each year.[4]

Interest payments on the bonds were originally scheduled to be due November 15 of each year. There is no penalty for the accelerated repayment of either principal or interest and the Department elected to prepay the entire $12.9 million in interest due on the bonds last year thereby relieving Colorado employers of future interest payments. In June, Fitch's Rating Service reaffirmed their original AA rating on the bonds citing Colorado's strong economic performance and anticipated ample revenue coverage for future principal payments.

**Current Trust Fund Outlook.** During the first quarter of each calendar year the Department produces a set of UITF forecasts that correspond to low, medium, and high growth economic scenarios. These forecasts are continually evaluated and updated throughout the year. The medium growth forecast, which has been closely tracking actual fund movements this year, is summarized below.

The current CDLE fund forecast is predicated upon moderate growth continuing through the 2019 forecast horizon. Annual job growth is assumed to average about 2 percent between 2014 and 2019 and unemployment fall from around 7 percent to 5 percent. Wages are projected to rise 3 percent on average during the forecast period.

Under these conditions fund reserves are anticipated to remain relatively stable through mid-2017 before expanding to over $1 billion by year-end 2019. The solvency or reserve ratio, a simple measure of the fund's financial soundness, will grow from 0.6 percent this year to 0.9 percent by 2019.[5] The last time the solvency ratio was at least 1.0 percent was

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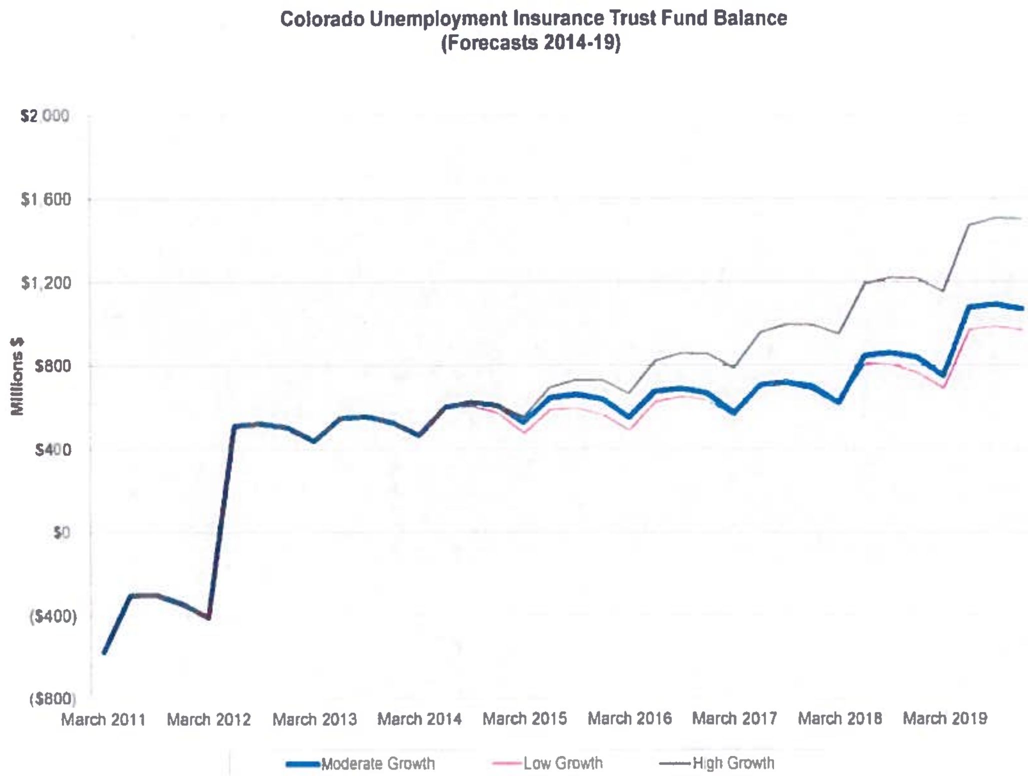
[4] The CDLE currently forecasts the bond principal surcharge to be approximately 20 percent each year through the life of the bonds. The surcharge is the estimated amount each employer's base premium must increase in order to equal the required annual principal payment of $125 million. The bond principal surcharge is expected to rise from about 22 percent this year to slightly more than 25 percent in 2015.

[5] The reserve ratio is the trust fund balance divided by annual total private wages. During past several recessions, a solvency ratio of about 1.4 percent measured from the start date of the recession would have been large enough to have allowed the fund to pay benefits without borrowing over the course of the

in 2001, just prior to the 2002-03 recession. The UITF is considered fully solvent for purposes of Colorado's premium rate structure when the adequacy ratio reaches 1.4 percent so that while the fund's solvency position is expected to improve through 2019 under medium growth conditions it will not attain fully funded status.




Employer contributions (including the from the bond principal surcharge) are forecast to increase marginally from $652.1 million in 2014 to $657.2 million in 2015 and vary between $630 million and $700 million through 2019. The taxable wage base, which is $11,700 in 2014, will increase to $11,800 in 2015 and $13,200 by 2019. The average premium rate is anticipated to decline from 0.69 percent to 0.51 percent over the forecast period. Annual interest earnings on fund reserves are anticipated to grow from $16.7 million this year to $31.9 million by 2019.

Benefits, meanwhile, are projected to remain relatively stable through 2019 as labor markets progressively tighten and unemployment shrinks. Benefit payments are expected to increase slightly from $500 million this year to $520 million in 2015 and about $540 million by 2019. The annual benefit cost rate will recede from 0.51 percent in 2014 to

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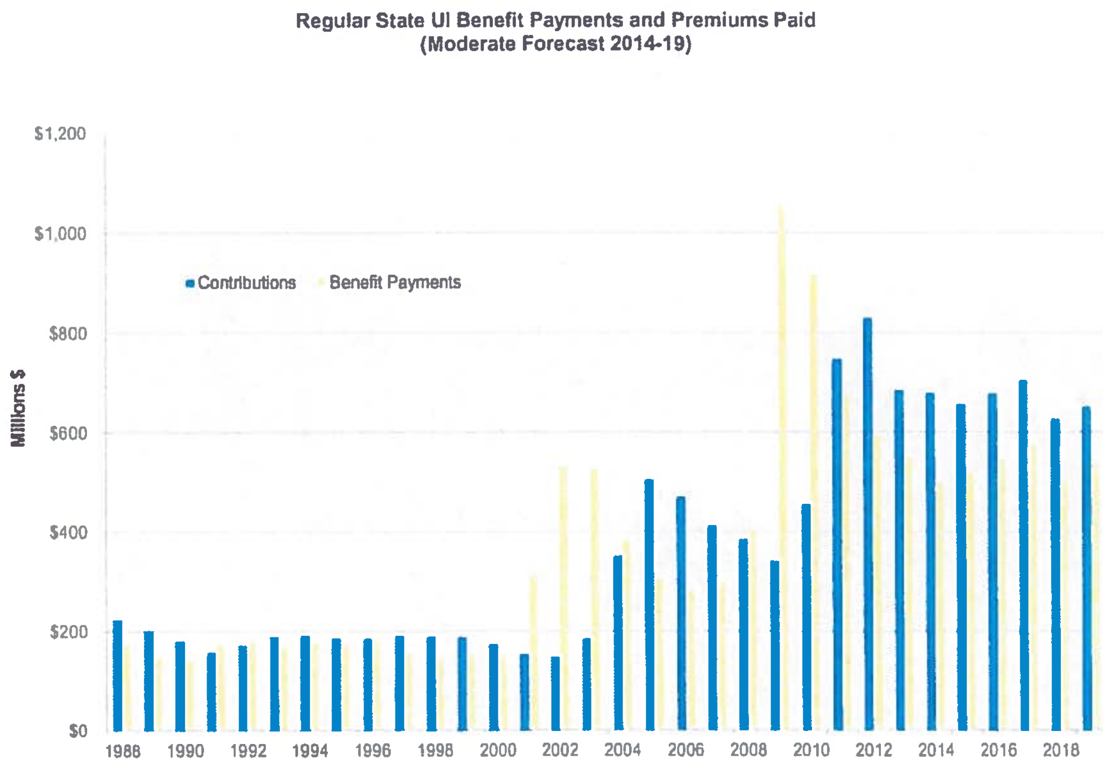
recession. The premium rate schedules adopted in HB11-1288 set employer premium rates at their minimum when fund reserves reach the desired 1.4 percent threshold.

0.42 percent by 2019.[6] The solvency surcharge, which had been assessed against Colorado employers since 2004, was turned off in 2013 as a result of UI bonding and is projected to remain off through the forecast period.




**Improper Payments.** Federal benefit-entitlement programs with improper-payment rates greater than 10 percent are considered to be out of compliance with federal performance standards.[7] In response to unacceptably high rates of improper-payments the CDLE established an Integrity Task Force (ITF) in 2011 whose task was to investigate the problem and recommend strategies to detect, prevent, and deter payment errors. As a result of the ITF's work, the CDLE has made considerable progress in reducing the rate of improper benefit payments the past several years. Between 2008 and 2011 Colorado's improper-payment rate was estimated to be 17 percent for a total of $305.4 million. However, from July 2013 through May 2014 the improper-payment rate after adjusting for recovered overpayments had shrunk to about 12.4 percent compared

[6] The average premium rate is total premiums divided by total private wages while the average benefit cost rate is benefit payments divided by expected total private wages. For comparison purposes, the average premium rate for the twenty-year period 1991-2010 was 0.44 percent and the average benefit cost rate was 0.57 percent. The highest annual benefit cost rate was 1.3 percent and occurred in 2009 when over a billion dollars was paid in benefits from the trust fund. The annual premium rate is expected to exceed the annual benefit cost rate through 2019 which means fund inflows (employer premiums received) are projected to exceed fund outflows (benefit payments).

[7] An improper-payment is one in which a claimant wrongly receives payment to which they are not entitled (overpayment) or is improperly denied payment to which they are entitled (underpayment). Approximately 96 percent of Colorado improper-payments between July 2013 and May 2014 were overpayments.

with 13.3 percent for the previous fiscal year. In dollar terms, the amount of improper payments fell from $84.7 million in fiscal year 2013 to about $78 million for fiscal year 2014.[8]

The following steps have been taken to detect and reduce the improper-payment rate:

- increase staff resources and training related to prevention and detection of overpayments;
- establish a targeted call campaign centered on claimants who report hours and earnings when filing for benefits;
- implementation of a computer software program to more quickly detect and take action when claimants do not report their earnings and receive benefits to which they are not entitled;
- implement operational changes to gather more complete and accurate information to improve decision-making quality;
- improve customer understanding of UI benefits requirements and responsibilities, including reporting new employment, earnings, job separations, other pay received, and work-search efforts;
- establishing a campaign to reach out to promote the use of electronic methods to respond to requests for information;
- implementation of the Treasury Offset Program to intercept federal tax refunds to recover improper payments caused by fraud or unreported earnings;
- implementation of a system that allows claimants to pay back their overpayments through debit- and credit cards.

In addition to lessening the rate of improper-payments the CDLE has made significant progress toward improving the overpayment collection rate. Just over $25 million in overpayments on the regular State UI program has been recovered from claimants since July 2012.

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[8] The $78 million is a prorated estimate based upon data for the first eleven months of the 2014 fiscal year.