COLORADO
Department of
Labor and Employment

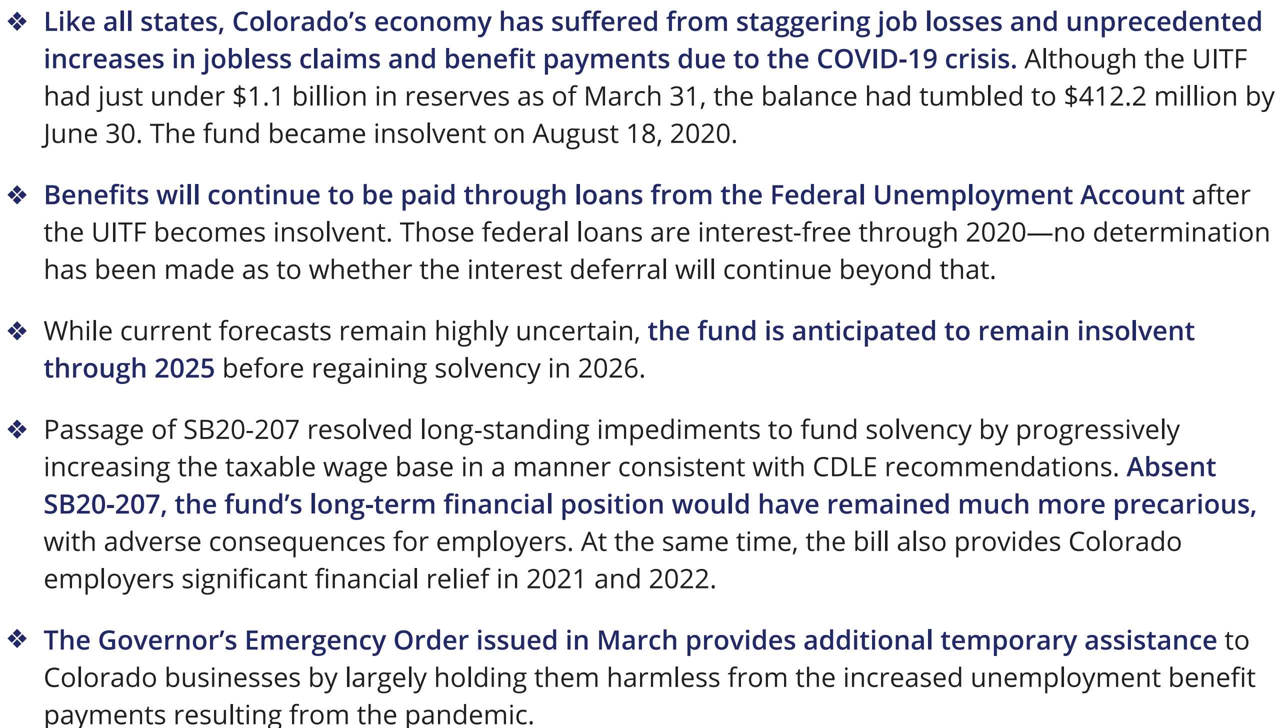
2020 COLORADO UNEMPLOYMENT INSURANCE TRUST FUND STATUS REPORT

COLORADO DEPARTMENT OF LABOR AND EMPLOYMENT
AUGUST 31, 2020

As required by HB11-1288, the Colorado Department of Labor and Employment (CDLE) produces an annual report on the financial condition of the unemployment trust fund (UITF) for the Colorado General Assembly by August 31.

01

EXECUTIVE SUMMARY



EXECUTIVE SUMMARY

- **Like all states, Colorado's economy has suffered from staggering job losses and unprecedented increases in jobless claims and benefit payments due to the COVID-19 crisis.** Although the UITF had just under $1.1 billion in reserves as of March 31, the balance had tumbled to $412.2 million by June 30. The fund became insolvent on August 18, 2020.
- **Benefits will continue to be paid through loans from the Federal Unemployment Account** after the UITF becomes insolvent. Those federal loans are interest-free through 2020—no determination has been made as to whether the interest deferral will continue beyond that.
- While current forecasts remain highly uncertain, **the fund is anticipated to remain insolvent through 2025** before regaining solvency in 2026.
- Passage of SB20-207 resolved long-standing impediments to fund solvency by progressively increasing the taxable wage base in a manner consistent with CDLE recommendations. **Absent SB20-207, the fund's long-term financial position would have remained much more precarious,** with adverse consequences for employers. At the same time, the bill also provides Colorado employers significant financial relief in 2021 and 2022.
- **The Governor's Emergency Order issued in March provides additional temporary assistance** to Colorado businesses by largely holding them harmless from the increased unemployment benefit payments resulting from the pandemic.

CALENDAR YEAR 2019 FUND STATUS

CALENDAR YEAR 2019 FUND STATUS

As of December 31, 2019, reserves held in the UITF totaled just over $1,121.0 million, an improvement of $188.1 million from twelve months earlier when the fund balance stood at $932.9 million.

Employer contributions paid into the UITF, including those from reimbursable employers, totaled $540.2 million during 2019, up slightly from $530.8 million the prior year. The increase in employer contributions resulted from strong wage growth that increased the taxable wage base to $13,100 from $12,600 in 2018 as well as continued employment growth. Those two factors offset a slight reduction in the average tax rate, which dipped from 0.41 percent in 2018 to 0.39 percent in 2019[1]. Interest earnings on fund reserves totaled $26.1 million in 2019 compared with $20.7 million in 2018.

At $370.7 million, 2019 regular unemployment insurance benefit payments were little changed from the $377.2 million paid in 2018. Average annual benefit payments 2016 through 2018 were $437 million. Just under 80,000 Coloradans received at least one unemployment insurance benefit payment in 2019, compared with almost 84,000 the previous year. Reflecting the tight labor market that held throughout 2019, the number of weeks paid to UI claimants in 2019 fell to its lowest level since 2000 and about 8 percent from the previous year. Over the past three calendar years, benefit payments have averaged about $437 million annually.

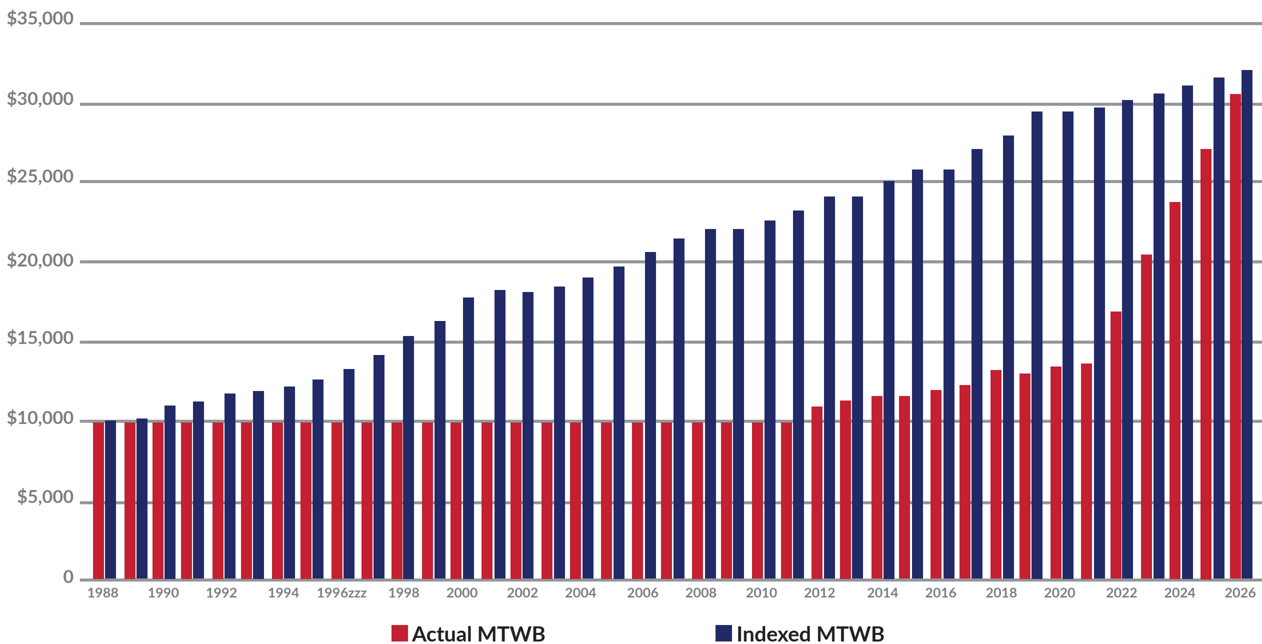
[1] Employer premium rates are determined by an employer's layoff history, the tax rate schedule in effect for that year, and any additional surcharges that may be in effect. The lengthy economic expansion that followed the Great Recession led to very low benefit charging against account employer accounts the past few years; consequently, most Colorado businesses had shifted to the low end of the premium rate schedule by 2019.

SB-207

SB20-207

The department has long noted and analyzed the deficiencies of the UI financing system stemming from an inadequate taxable wage base level.[2] SB20-207 remedies what had been an intractable obstacle to long-term sustainable fund solvency by incrementally raising the wage base from its current level of $13,600 to $30,600 by 2026.[3] This will bring the base very close, relative to average annual earnings, to the level that existed in 1988 (see graph below). Doing so changes the structure of the fund from a deficit-financing arrangement to a more desirable forward-financing structure. These increases in the wage base are the most meaningful since the 1980s when the base was raised several times after the UITF became insolvent following the severe recessions of the early 1980s.

Actual vs. Hypothetical Indexed Maximum Taxable Wage Base 1998–2026 (2021-2026 established by SB20-207)



[2] The problem related to the wage base has been described in prior status reports.

[3] Under SB20-207, the wage base is frozen at $13,600 in 2021 and increases to $17,000 in 2022; $20,400 in 2023; $23,800 in 2024; $27,200 in 2025; and $30,600 in 2026. The wage base will resume being indexed to the annual change in covered earnings after 2026. Other aspects of the bill, such as those related to the treatment of independent contractors and earnings offsets to benefits are not considered here.

Recognizing the economic stress to businesses caused by the pandemic, SB20-207 delays the first incremental increase to the taxable wage base until 2022. Importantly, the bill also freezes the wage base at $13,600 for 2021 and eliminates the employer solvency surcharge for 2021 and 2022. We estimate the latter two provisions will save Colorado employers a total of $190 million in premiums in 2021 and 2022.[4]

While suspending the solvency surcharge and freezing the wage base will aggravate fund insolvency over the next two years, the long-term impacts of SB20-207 will be very positive for fund solvency. As the increases to the wage base are phased-in, they will substantially lessen trust fund deficits over the forecast period—a forecast comparison shows an approximate $1 billion improvement in the trust fund balance by 2025 due to SB20-207. The improvement will not only reduce potential interest costs related to borrowing but also greatly accelerate the fund's return to solvency, which will reduce employer premium rates. Once the economy enters the next sustained growth cycle, the benefits to employers will accrue more quickly because the higher fund balances will gradually shift employers to lower premium rate schedules.

Raising the wage base also promotes greater tax equity between high- and low-wage employers. Because the wage base in Colorado has remained depressed relative to average earnings for so many years, the financing inequity between low and high paying businesses has steadily worsened. By expanding the base, SB20-207 addresses this issue.[5]

For some purposes, the UITF is considered fully solvent once the June 30 reserve ratio reaches at least 1.4 percent. SB20-207 requires CDLE to reduce employer premiums up to 15 percent once this measure of full solvency is attained. However, the fund is not expected to reach this benchmark over the forecast horizon.

[4] The taxable wage base was scheduled to increase to $14,300 in 2021. The solvency surcharge triggers on the following January when the reserve ratio (also referred to as the solvency ratio) falls below 0.5 percent. The reserve ratio, which is one way of measuring fund solvency, is the June 30 trust fund balance divided by the prior year's total wages paid to UI covered workers.

[5] Consider a low wage employer, L, and a high wage employer, H, each with five employees and each having a premium rate of one percent. Suppose the wage base is $13,600 and L pays its workers $13,600 annually while H pays its workers $100,000. Then L and H are each assessed an identical UI tax of $13,600 x 5 x 0.01 or $680. However, the average tax on total wages is one percent for L ($680/$68,000) but only 0.136 percent for H ($680/$500,000)—i.e., H's average rate is less than one-seventh of L's. With a wage base of $30,000 the average rate for L remains unchanged but the rate for H increases to 0.3 percent, narrowing the difference between the two to just under one-third. Large employers tend to pay higher wages than small businesses so that the inequity is really one between large and small employers.

04

GOVERNOR'S EMERGENCY ORDER & UNEMPLOYMENT EXPERIENCE RATING

GOVERNOR'S EMERGENCY ORDER & UNEMPLOYMENT EXPERIENCE RATING

Federal law requires that states link an employer's unemployment tax rate with the employer's layoff history, a process known as experience rating. The specific way in which this is accomplished varies among states but the process generally involves comparing the unemployment benefits charged against an employer to the unemployment taxes paid by that employer. Employers who pay more in taxes than have benefits charged against their accounts have lower rates than those whose benefits exceed taxes paid into the unemployment system. As layoffs rise during the course of a recession, benefit charging also increases, and the experience-rate process shifts more businesses toward higher premium rates. As the economy begins to recover, those higher premium rates, combined with a decline in benefit payments, allows the trust fund to begin rebuilding reserves. Over time, as a recovery is sustained and strengthens, employers shift to lower premium rates, and as the trust fund balance grows, all employers move to lower rate schedules[6] Colorado's lengthy and robust expansion since the Great Recession resulted in the large majority of Colorado businesses having shifted to low premium rates.

Under the Governor's Emergency Order issued in March related to the COVID pandemic, unemployment benefits normally charged against an employer's account will be charged instead to the UITF. Charging benefits directly to the UITF rather than against individual businesses will prevent pandemic-related layoffs from having an adverse effect upon premium rates, essentially holding Colorado businesses harmless.[7]

CDLE has not determined how long socialization of benefit charging will remain in place. The department is currently considering suspending employer benefit charging through the end of 2020, but may shorten or extend the date depending upon how rapidly public health conditions allow for a return to more normal social and economic activities. It is important to note that while employers will see some premium relief, this action will have negative, although indeterminate, consequences for fund solvency.

[6] Employer premium rates in Colorado are set once a year and take effect each January. The taxes and benefits incorporated into an employer's experience-rate are based upon activity that occurs during the twelve-month period ending the previous June 30, which means that rate setting operates with a lag. It generally takes about three years for the increased benefit charging that occurs during recessions to begin significantly affecting employer premium rates.

[7] Because employer rates are also determined by the trust fund balance, all employers will move to higher premium rate schedules as fund reserves are depleted. Although benefit charging against individual employer accounts has been temporarily suspended, employers are still being credited with the premiums paid into their accounts—the net effect for many businesses will be to improve, rather than simply hold harmless, their experience-rating for some period.

IMPROPER PAYMENTS

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.[8] The Department's Integrity Task Force (ITF) is charged with analyzing the issues, root causes, and trends related to improper payments. Based on analysis and input, ITF recommends strategies to detect, prevent, and deter payment errors. Improper payment data are provided to the USDOL, which tracks the improper payment rate annually based on a small sample size of paid claims within that year. CDLE continues to make great strides in improving its performance in this area. For calendar year 2019, CDLE exceeded the federal performance standard. The gross improper payment rate for calendar year 2019 was 8.91 percent, while the net improper payment rate was 6.67 percent. The net improper payment rate is calculated by subtracting recovered overpayments from the estimated gross improper payment rate.

Most improper payments are the result of claimants not meeting their eligibility requirements, failing to provide information as required, providing incomplete or inaccurate information, and/or employers failing to provide information as required or providing incomplete or inaccurate information. As a result, efforts to reduce improper payments have been focused on communication and education of requirements and responsibilities as well as technology upgrades designed to gather more complete and accurate information needed to make a proper determination to pay benefits.

In addition to these efforts, the CDLE is on the verge of implementing a new, modernized computer system that will improve the accuracy and completeness of information received, as well as legislative changes regarding other remuneration and earnings that should positively impact the improper-payment rate.

In addition to lessening the rate of improper payments, CDLE has made significant progress toward improving the overpayment collection rate. Between 2012 and 2019, over $86.8 million in overpayments on the regular State UI program was recovered from claimants.

[8] 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 93.3 percent of Colorado improper payments in 2019 were overpayments.

TRUST FUND OUTLOOK

TRUST FUND OUTLOOK

In May and June, the nation regained about a third of the 20 million nonfarm jobs lost in April. However, while employment began rebounding in May and June following a resumption of business activity in many states, the surge in COVID cases that followed has since led to widespread business reclosures. Many establishments that shut temporarily are unlikely to reopen, and the number of high profile business bankruptcies continues to rise. Even in areas that continue to stay open, workers are likely to see reductions in both hours and wages as the effects spread to parts of the economy that were not initially directly affected by business closings. State and local governments, which typically rely upon sales, property, and personal income taxes to fund services, have collectively shed more than 1.5 million jobs since March. Many of the layoffs in both the public and private sector are thus far classified as temporary but it is probable that a significant share of these job losses will become permanent.

Between February and June, Colorado's jobless rate skyrocketed from 2.5 percent to 10.5 percent while nonfarm payrolls shrunk by 220,000.[9] The share of working Coloradans age 16 and greater plummeted from 67.7 percent in February to 61.4 percent in June, a decline unmatched over any post-World War II period.

In response to the pandemic, Congress established the Pandemic Unemployment Assistance program (PUA), which allows payment of unemployment benefits to the large group of individuals who are ineligible for benefits under traditional unemployment programs (self-employed, contingent, and temporary workers). Because the federal government funds PUA benefits they have no impact upon state trust funds. All persons who receive unemployment benefits, whether covered under PUA or regular state unemployment programs, also receive an additional $600 in weekly benefits. This additional $600 weekly benefit, known as Federal Pandemic Unemployment Compensation (FPUC), was also federally paid but expired at the end of July.

[9] These figures are seasonally adjusted. Due to respondent and misclassification errors, the true jobless rate is likely several percentage points higher than the official rate. The more expansive household survey based definition of employment shows a decline of 270,000.

06 TRUST FUND OUTLOOK

Since the end of March, Colorado has paid more than $1.3 billion in regular state unemployment payments, $428 million in PUA benefits, and $2 billion in FPUC benefits. Congress also allowed states meeting certain conditions to qualify for federal reimbursement of a claimant's first week of benefits through 2020.[10] The State has so far received more than $150 million for payment of the first benefit week. The number of persons receiving a payment from Colorado's regular unemployment system totaled nearly 280,000 in June, up from about 25,000 in February. Coloradans receiving a PUA benefit numbered roughly 97,000.

Because the economy is likely to recover in fits and starts for an extended time, the trust fund forecasts contain a large degree of uncertainty. The Fed has clearly expressed its intention of maintaining a low-interest rate environment indefinitely, including the support of private business borrowing through its corporate bond purchase program. Future federal fiscal policy responses, however, such as extension of the Payroll Protection Program, additional federal assistance for state and local governments, and re-authorization of the various federally paid unemployment compensation programs, remain unclear.

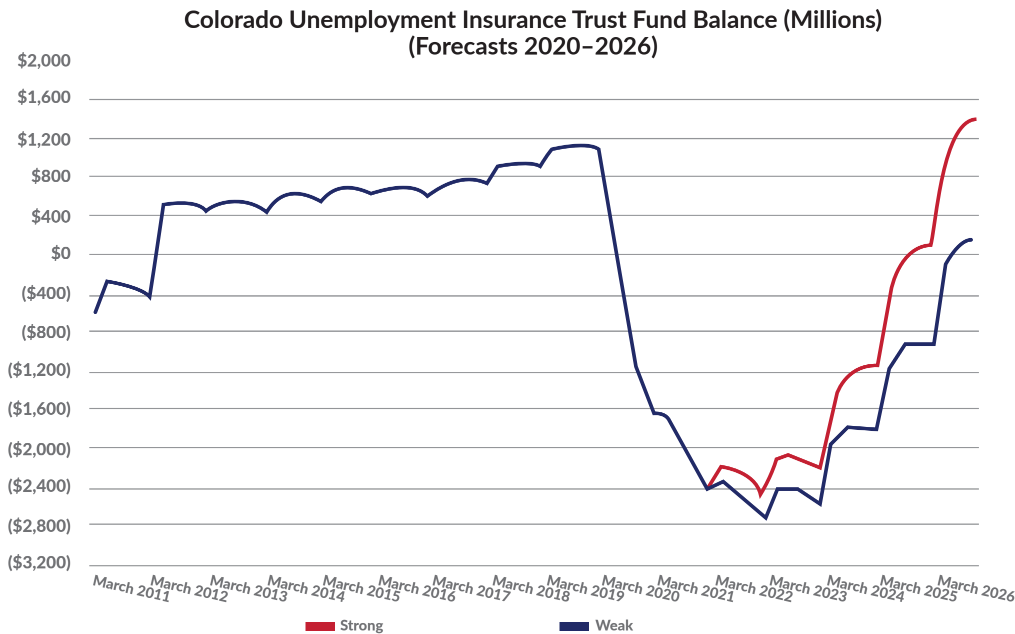
For now, the Department is using two forecasts that will be continually updated throughout the year—one based upon a relatively strong recovery, and one predicated upon economic conditions remaining subdued through 2026. The forecasts incorporate the provisions of SB207 related to increases in the wage base beginning 2022, suspension of the solvency surcharge in 2021 and 2022, and the freeze in the wage base for 2021. The strong forecast assumes weak labor market conditions through 2021 but assumes all jobs lost in 2020 and 2021 are regained by 2023; the weak forecast assumes employment losses will not be recaptured until after 2025. The insured unemployment rate, a measure that reflects the degree of strain upon the trust fund, is anticipated to average 8 percent in 2020 and 3 percent in 2021 in both scenarios.[11]

Update as of August 24, 2020:
The trust fund became insolvent with a zero balance on Tuesday, August 18, 2020. The department began drawing on a line of credit with the United States Treasury. This borrowing is at zero interest until December 31, 2020 per the CARES Act.

[10] Because many claimants return to work quickly after having been laid-off, in most states the first week of unemployment compensation is not paid—this week is known as the waiting week. Because the number of job openings evaporated during the pandemic, the federally government is now paying for the waiting week.

[11] By contrast, the insured unemployment rate averaged 3.11 percent during 2009, the peak of the Great Recession. The insured unemployment rate can be thought of as the jobless rate for individuals covered under unemployment insurance while the more familiar total unemployment rate measures the unemployment rate for all workers, regardless of their attachment to the unemployment insurance system.

06 TRUST FUND OUTLOOK



The number of benefit weeks paid under the regular UI program are forecast to exceed eight million in 2020—by comparison, during the peak years of the Great Recession in 2009 and 2010 the number of weeks paid never topped three million. Benefits paid from the UITF are expected to total $2.9 billion in 2020 and $1.4 billion in 2021 before dropping to roughly $800 million between 2022 and 2026. Under these conditions, the fund will become insolvent August 2020 and reach its maximum level of insolvency, around $2.7 billion, in early 2023.[12] In both the strong and weak recovery scenarios, the fund would become solvent again in 2026. The weak forecast has the 2026 year-end fund balance reaching $146 million while the strong forecast shows a balance of about $1.4 billion. The solvency surcharge is expected to be in effect 2022 through 2026.

Colorado borrowed about $1.1 billion in total from the Federal Unemployment Account (FUA) between 2010 and 2012 to pay benefits on the state unemployment program. FUA borrowing permits states considerable flexibility with respect to the timing of principal repayment although the costs associated with FUA borrowing begin to increase after several years. Ten states are currently using interest-free federal advances to pay unemployment benefits and another eight states, including Colorado, have established lines-of-credit in anticipation of borrowing. It is expected the number of states utilizing FUA advances will grow substantially as the economic shock from the pandemic persists.

[12] States whose trust funds become insolvent may borrow interest-free from the Federal Unemployment Account through 2020 to pay unemployment benefits. At this time, no decision has been made as to whether federal interest-free advances will continue beyond 2020.