

South Carolina Unemployment Insurance Trust Fund Annual Assessment FY2015

Executive Summary

For each fiscal year, the South Carolina Department of Employment and Workforce is required to submit, by October 1st, a report to the Governor, General Assembly and the Review Committee indicating the amount in the Unemployment Insurance (UI) Trust Fund and making an assessment of its funding level in accordance with Section 41-33-45 of the South Carolina Code of Laws.

Current Status

Unemployment benefit outlays for FY2015 totaled \$193,065,875¹. Revenues generated to fund the unemployment insurance programs (including for the benefit outlays, loan repayments and interest repayment) totaled \$428,886,783².

As of June 30, 2015, the Unemployment Compensation Trust Fund had a positive adjusted balance of \$280,378,541³. The health of the trust fund has improved substantially over the past fiscal year with all federal loans being repaid prior to the end of the fiscal year.

Since April 2011, the state has not had to borrow any funds from the federal government to make benefit payments. The final payment on the federal loans occurred on June 11, 2015. During this period South Carolina obtained the maximum Federal Unemployment Tax Act (FUTA) credit for its businesses (i.e., 2011, 2012, 2013, 2014, and 2015). Moreover, South Carolina was able to make either early or voluntary repayments of the federal loan that resulted in another \$12-13 million in interest savings for South Carolina businesses helping to reduce taxes for CY2014 compared to prior years.

Future Outlook

Based on current economic conditions, it is projected that approximately \$207.5 million in state UI benefits will be paid in FY2016. Per SC Code Ann. § 41-27-380, the taxable wage base increased in January 2015 to \$14,000. It should be noted that this increase in the taxable wage base will not necessarily increase the amount of taxes collected, but rather spread the taxation across a greater amount of wages and period of time. The projection for benefit contributions to be raised in FY2016 is \$358.5 million -- to cover FY2016 benefit outlays and the beginning of trust fund rebuilding, per SC Code of Law Ann. §41-31-45(C) and SC Code of Regulations 47-501.

¹ Annual Trust Fund Report

² *Ibid*

³ This audited trust fund balance includes cash deposited in the state's unemployment trust fund, clearing and benefits payment account, advances from the federal government, amounts due and payable as a payment in lieu of contributions by a non-profit organization, and any contributions and interest received **by July 31st**.

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South Carolina Unemployment Insurance Trust Fund Annual Assessment FY2015

Current Unemployment Compensation Fund Status

The adjusted Unemployment Compensation Fund balance as of June 30, 2015 was \$280,378,541⁴. No federal advances (i.e., the loans) were needed to pay state UI benefits during FY2015. All advances from the federal government were repaid as of June 30, 2015.

Recent Unemployment Compensation Fund History

Historical data of the principal components of the state Unemployment Trust Fund are outlined in Table 1. Graphs of the historical contributions, benefits, and fund balance are shown in Figure 1.

Table 1: Unemployment Compensation Fund Components, FY2010-2015⁵

| Component | FY2010 | FY2011 | FY2012 | FY2013 | FY2014 | FY2015 |
|------------------------|--|--------------|-------------------------|--------------|--------------|--------------|
| Advances | 541,780,847 | 115,174,767 | 0 | 0 | 0 | 0 |
| Contributions | 289,312,460 | 508,568,694 | 388,907,57 ⁶ | 411,039,535 | 486,539,699 | 428,886,783 |
| Earned Interest | Interest not earned while Trust Fund is in Debt Status | | | | | 745,382 |
| Benefits | 776,761,390 | 502,607,650 | 410,431,401 | 258,801,120 | 231,775,670 | 193,065,875 |
| Fund Balance | 104,890,659 | 323,207,676 | 326,883,925 | 328,787,740 | 365,801,884 | 280,378,541 |
| Total Wages | 49.3 billion | 51.9 billion | 54.0 billion | 55.1 billion | 58.5 billion | 61.6 billion |

Note: Certain adjustments have been made to correctly carry-forward prior year balance.

The components of the Trust Fund are defined as follows:

- Advances – Funds received from the US Department of Labor to make benefit payments.
- Contributions – Contributions received from employers as of June 30th.
- Interest – Federal Treasury interest posted to each state’s Trust Fund account quarterly.⁷
- Benefits – State funded benefit payments less benefit overpayment recoveries.
- Fund Balance – Adjusted Trust Fund balance
- Total Wages – Total covered payroll wages reported by all covered employers for the period beginning July 1 and ending June 30.

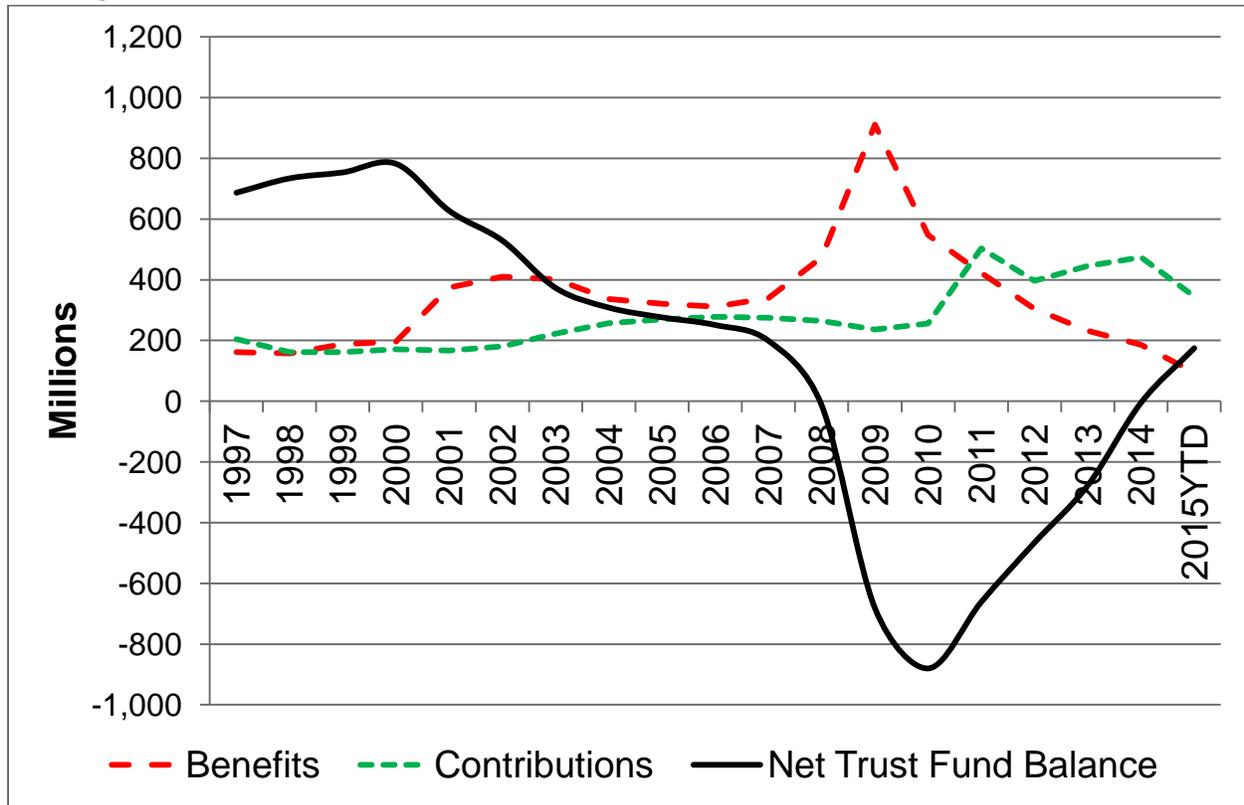
⁴ Trust fund balance includes cash deposited in the state’s unemployment trust fund, clearing and benefit payment accounts, advances from the federal government, amounts due and payable as a payment in lieu of contributions by a non-profit organization, and any contributions and interest received by July 31st, per SC State Code 41-31-80.

⁵ By state fiscal year; **not** cumulative

⁶ FY2012 contributions are lower due to the rate recalculation associated with General Fund appropriations that led to a significant level of credits and refunds issued

⁷ No interest is due to the state Trust Fund account from the Federal Treasury when federal advances remain outstanding.

Figure 1: Historical Contributions, Benefits, and Fund Balance, CY1997-2015⁸

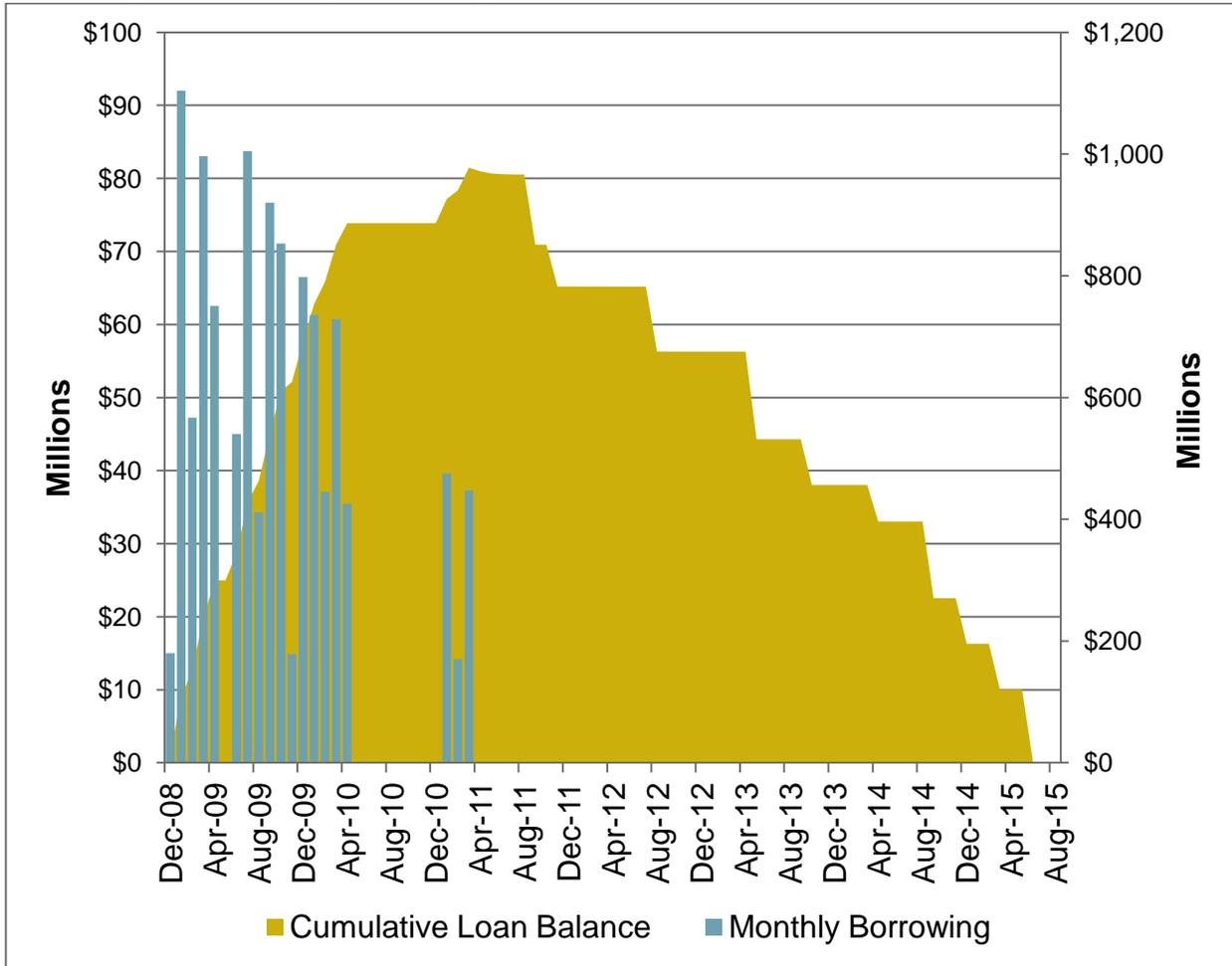


Overview of Advances

The UI Trust Fund became insolvent in December 2008 and was required to draw significant federal unemployment advances between December 2008 and April 2010. Additional federal advances were required between January and April 2011. Figure 2 shows the borrowing by month since December 2008. An improvement in the economy, higher than anticipated contributions in the last half of FY2010, a one-time infusion of incentive funding from the federal Department of Labor, and the new tax structure have all combined to allow the trust fund to reduce borrowing between April 2010 and April 2011. Since April 2011, no additional federal loans have been necessary to fund the benefit payments.

⁸ US Department of Labor: Financial Handbook 394 (information from USDOL excludes all federal advances and other fiscal year-ending adjustments)

Figure 2: Monthly Borrowing and Cumulative Loan Balance, Dec 2008 - Sep 2015



Solvency Standards

South Carolina has adopted the most widely accepted measure of trust fund solvency, known as the Average High Cost Multiple (AHCM). See S.C. Code Ann. § 41-31-45(A). This measure of whether a state has enough money to cover unemployment claims during an economic downturn was devised in 1995 by the federal Advisory Council on Unemployment Compensation.

The AHCM is calculated by taking the trust fund balance as a percent of estimated wages for the most recent 12 months (also known as the reserve ratio) and dividing it by the Average High Cost Rate, which is the average of the three highest calendar year benefit cost rates, in the last 20 years or a period including three recessions, whichever is longer. Benefit cost rates are benefits paid as a percent of total wages in taxable employment.

The Department of Labor recommends that a state have an AHCM of 1.0, which means that the state has enough funds to pay one year of benefits at the Average High Cost. This should be sufficient to fund benefits during a moderate recession. Pursuant to state law, the agency promulgated new regulations, 47-500 and 47-501, to return the trust fund to an adequate balance within 5 years. As of

June 30, 2015, the state trust fund on deposit with the US Treasury had a positive balance of \$175.2 million, (\$202.4 million, including authorized interest transfer.)⁹

Table 2 shows South Carolina's three highest benefit cost rate years, the state's actual (or projected) total wages, and the trust fund balance that would be required to achieve the recommended solvency level of 1.0.

Table 2: Solvency Standards and Projections¹⁰

| Calendar Year | High Cost Years | Average High Cost Rate | Total Wages prior year (billions\$) | Target Balance (AHCM=1.0) (millions\$) |
|----------------------|------------------------|-------------------------------|--|---|
| 2013 | 1991, 2009, 2010 | 1.30 | \$52.8 | \$689.3 |
| 2014 | 1991, 2009, 2010 | 1.30 | \$55.1 | \$718.6 |
| 2015 | 1991, 2009, 2010 | 1.30 | \$57.0 | \$743.7 |
| 2016 | 1991, 2009, 2010 | 1.30 | \$60.2 | \$785.3 |
| 2017 | 1991, 2009, 2010 | 1.30 | \$62.6 | \$816.7 |
| 2018 | 1991, 2009, 2010 | 1.30 | \$65.1 | \$849.3 |
| 2019 | 1991, 2009, 2010 | 1.30 | \$67.7 | \$883.3 |
| 2020 | 1991, 2009, 2010 | 1.30 | \$70.4 | \$918.6 |

Projections in italics

Since all federal loans have been repaid as of the end of FY2015, trust fund rebuilding will continue until reserves are sufficient to support an AHCM of 1.0, as recommended by the DOL and required by S.C. Code Ann. § 41-31-45(A)(1). For 2016 the fund adequacy target is projected to be \$785.3 million based on total wages paid in the prior year of \$60.2 billion and an average high cost rate of 1.3.

Transparency of Funding (Proviso 83.4)

In accordance with FY2015-16 Appropriations Act Proviso 83.4 this report also provides information on 1) state unemployment taxes collected by tax class, 2) unemployment benefit claims paid, 3) number and dollar value of improper unemployment benefits paid, 4) payments made to the federal government for outstanding unemployment benefit loans, and 5) the balance in the state's Unemployment Trust Fund at fiscal year's end.

Tax Collections by Tax Class

Tax rates are set on a calendar year basis in the late fall of each year. Tax rates for CY2015 were set in October 2014.

In CY2014, a total of \$462.1 million was collected in the form of total state unemployment taxes. These funds were used to pay unemployment benefits to eligible individuals who were laid off through no fault of their own, to make required loan repayments to the federal government for South Carolina's current outstanding unemployment debt, and to make interest payments on that outstanding loan balance. In addition to the base tax rate for benefit and loan payments and the

⁹ This is the balance on deposit with the US Treasury and does not reflect any amounts in the clearing or benefit payment accounts. The Trust Fund audited balance of \$280.4 million includes deposits received after June 30, 2015 as well as amounts due and payable from reimbursable employers.

¹⁰ US Department of Labor: Financial Handbook 394

interest surcharge for interest payments, all businesses in the state are also responsible for paying a 0.06% administrative contingency assessment.

Table 3 shows the contributions paid for CY2014 by each tax class.

Table 3: Contributions by Tax Rate Class, 2014¹¹

| Tax Rate Class | # Liable Businesses | Base Tax Contributions | Interest and Contingency Contributions | % of Total Contributions |
|-----------------------|----------------------------|-------------------------------|---|---------------------------------|
| 1 | 57,759 | \$189,658 | \$2,300,112 | 0.5% |
| 2 | 945 | \$5,026,216 | \$700,142 | 1.2% |
| 3 | 687 | \$5,554,930 | \$736,540 | 1.4% |
| 4 | 709 | \$5,375,797 | \$670,668 | 1.3% |
| 5 | 940 | \$6,578,024 | \$755,473 | 1.6% |
| 6 | 816 | \$7,316,489 | \$813,589 | 1.8% |
| 7 | 643 | \$8,963,944 | \$945,109 | 2.1% |
| 8 | 798 | \$7,996,637 | \$796,641 | 1.9% |
| 9 | 599 | \$9,711,148 | \$926,598 | 2.3% |
| 10 | 920 | \$11,416,986 | \$1,039,809 | 2.7% |
| 11 | 1,186 | \$11,805,078 | \$1,026,174 | 2.8% |
| 12 | 25,726 | \$28,051,512 | \$2,350,506 | 6.6% |
| 13 | 1,257 | \$25,888,668 | \$1,790,498 | 6.0% |
| 14 | 1,305 | \$29,169,924 | \$1,960,583 | 6.7% |
| 15 | 1,599 | \$32,808,131 | \$2,152,859 | 7.6% |
| 16 | 2,088 | \$34,938,714 | \$2,242,024 | 8.0% |
| 17 | 2,249 | \$42,608,355 | \$2,695,662 | 9.8% |
| 18 | 2,441 | \$39,184,923 | \$2,434,246 | 9.0% |
| 19 | 3,019 | \$50,174,792 | \$3,072,328 | 11.5% |
| 20 | 11,169 | \$66,006,545 | \$3,917,926 | 15.1% |
| TOTAL | 116,855 | \$428,766,469 | \$33,327,487 | |

While there are a large number of liable businesses in rate class 1, these are relatively small in size. Approximately 5 percent of the state's taxable wages (excluding new businesses) are assigned to each category. Businesses with less than 12 months of liability are assigned a new business tax rate of class 12. This accounts for the large volume of businesses in that category in Table 3. Any business with a delinquent wage and contribution report or who has delinquent unemployment taxes due to the agency are assigned to rate class 20, which accounts for the larger volume of businesses in that category as well.

Unemployment Benefits Paid

State unemployment taxes fund up to the first 20 weeks of unemployment benefits to individuals who are out of work. Prior to June 2011, the state unemployment taxes funded up to the first 26 weeks of unemployment benefits. Due to the reduction in the number of available weeks, continued job growth,

¹¹ Internal reports of CY2014 contributions, contingency, and interest surcharge payments by tax class as of August 12, 2015.

economic improvement in the state, and stricter disqualification penalties being implemented, benefit payments have come down substantially from their height in 2009.

Figure 3 shows the state-funded benefits paid by month from January 2008 through August 2015. Monthly benefit payments reached a peak in March 2009 at over \$98 million. In the most recent month available from the United States Department of Labor (DOL), benefit payments had dropped to slightly over \$12.6 million, an 87.2 percent drop. Benefit payments have leveled off in recent months as the unemployment rate has remained around the 6.4 percent mark. Benefits can be expected to decline as the number of unemployed individuals falls and job growth increases.

Figure 3: Monthly State-Funded Unemployment Benefit Payments, Jan 2008 – Aug 2015¹²



Unemployment Insurance Improper Payments

The Fraud, Investigation, Recovery, and Enforcement (FIRE) Unit is responsible for preventing, detecting and recouping any improper payments to claimants from the UI program while the Benefit Accuracy Measurement (BAM) Unit is responsible for estimating the percentage of improper payments through sampling of claims. Table 4 provides information on the estimated level of improper payments for South Carolina for the most recent fiscal year as well as the cause of the improper payment.

¹² United States Department of Labor, <http://workforcesecurity.doleta.gov/unemploy/claimssum.asp>

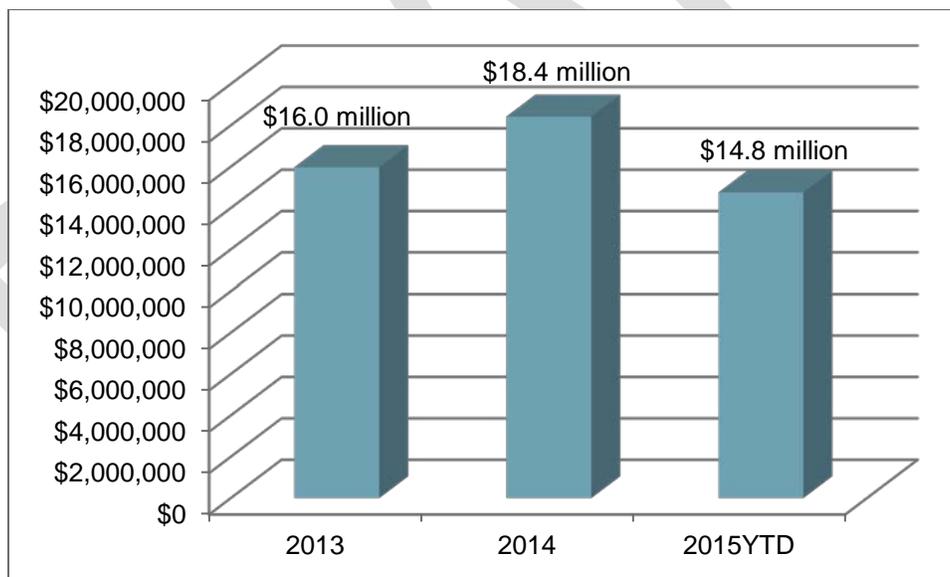
Table 4: Improper Payments Estimates, 2014Q3-2015Q2¹³

| | Sample Size | Improper Payment Rate | Est. Dollars Overpaid |
|------------------------------|-------------|-----------------------|-----------------------|
| Total | 504 | 17.4% | \$33.8m |
| Benefit Year Earnings | | | \$13.0m (38.5%) |
| Work Search Issues | | | \$12.1m (35.7%) |
| Separation Issues | | | \$4.9m (14.4%) |
| Eligibility Issues | | | \$3.5m (10.5%) |
| All Other | | | \$0.3m (0.9%) |

The majority of improper payments are caused by claimants continuing to file for benefits after they return to work and failing to report their earnings. In the FY2015, this accounted for over 38% of all improper payments, or \$13.0 million.

The agency has several means of collecting any overpayments made to claimants. Some of the most successful include the federal and state income tax refund intercept programs (TOPs and SOD). Involuntary wage withholding after the claimant returns to work is another avenue to collect from individuals who do not repay their overpayments or fail to enter into repayment agreements. Overpaid individuals also have the option to repay their benefits securely and easily online.

Figure 4: Overpayment Collections¹⁴



UI Loan Payments

Between December 2008 and April 2011, the State of South Carolina borrowed over \$1 billion from the federal government to continue funding unemployment benefits. The state unemployment tax system underwent a dramatic overhaul in 2011 that allowed South Carolina to cease all borrowing in April 2011. In September 2011, South Carolina made its first voluntary repayment to the federal

¹³ Based on BAM Findings Annual Report Range 201427-201526

¹⁴ Internal reports as of 8-20-15; includes state and federal tax intercepts and wage withholding

government. Figure 2 shows the monthly loans taken by DEW and the cumulative loan from 2008 to present.

As of June 11, 2015, all loans were repaid to the federal government through a combination of a one-time increase in federal taxes for tax year 2010 and 10 voluntary payments made between 2011 and 2015. Table 5 provides detailed repayment information.

Table 5: South Carolina UI Loan Payments, April 2011 – September 2015¹⁵

| Date | Payment(millions) | Reason |
|----------------|-------------------|--|
| Apr-Aug 2011 | \$35.30 | Increased federal tax required in 2010 ¹⁶ |
| Sep-11 | \$115.2 | Voluntary Payment |
| Nov-11 | \$68.8 | Voluntary Payment |
| Mar-Jun 2012 | \$0.3 | Increased federal tax required in 2010 |
| Aug-12 | \$106.5 | Voluntary Payment |
| Dec-12 | \$0.004 | Increased federal tax required in 2010 |
| Mar-13 | \$0.01 | Increased federal tax required in 2010 |
| May-13 | \$144.02 | Voluntary Payment |
| Jun- July 2013 | \$0.0034 | Increased federal tax required in 2010 |
| Oct-13 | \$75 | Voluntary Payment |
| Nov-Dec 2013 | \$0.012 | Increased federal tax required in 2010 |
| Apr-14 | \$60 | Voluntary Payment |
| May-Aug 2014 | \$0.024 | Increased federal tax required in 2010 |
| Sep-14 | \$126 | Voluntary Payment |
| Nov-14 | \$0.001 | Increased federal tax required in 2010 |
| Dec-14 | \$75.00 | Voluntary Payment |
| Jan-15 | \$0.013 | Increased federal tax required in 2010 |
| Mar-15 | \$75.00 | Voluntary Payment |
| Jun-15 | \$120.50 | Voluntary Payment |
| TOTAL | \$1,001.70 | |

Trust Fund Balance

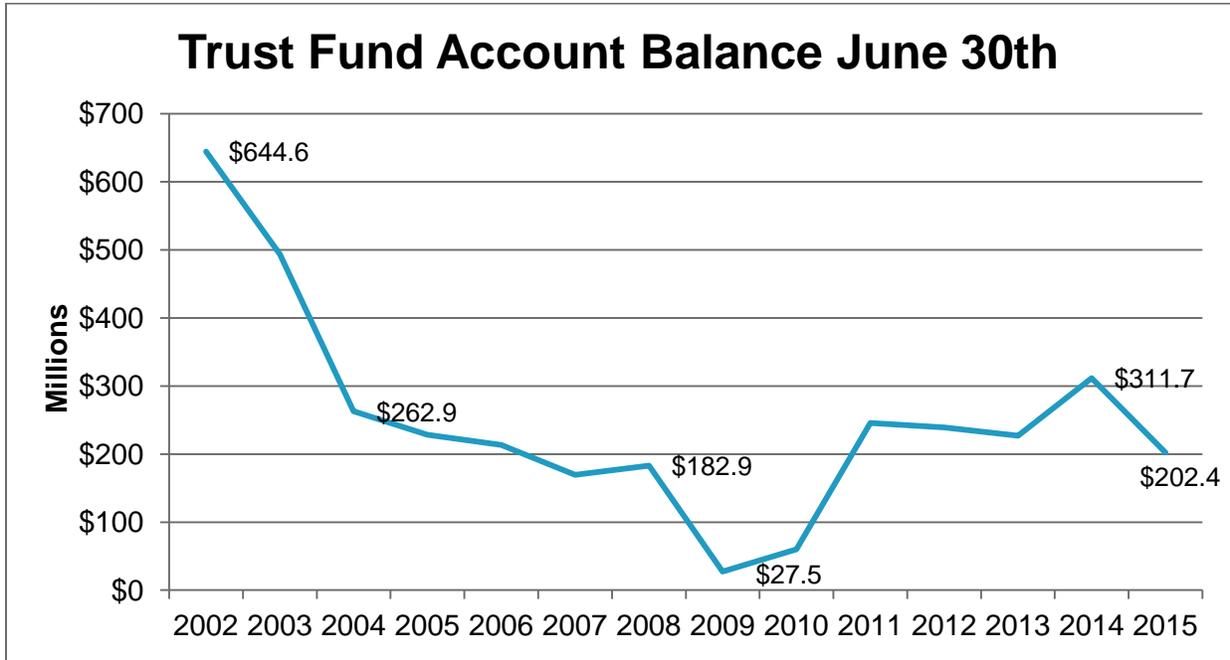
As of June 30, 2015 there was a balance of \$175,177,167 (\$202,430,856 including the authorized interest transfer),¹⁷ in the state's unemployment trust fund held at the US Treasury in Washington DC. As shown in Figure 5, the balance in the UI Trust Fund declined steadily between June 30, 2002 and June 30, 2011 but has recovered over the past four years. Not shown is that these balances include loans between 2009 and 2015. The trust fund balance as of June 30, 2015 does not include any outstanding loans as they were repaid in full on June 11th. The timing of the last loan payment accounts for the lower trust fund total in 2015 compared to 2014.

¹⁵ Treasury Direct Monthly Statements

¹⁶ For tax year 2010, SC employers experienced a 0.3% point increase in their federal unemployment taxes due to the outstanding federal loan. This additional tax collection was sent from the IRS to the federal Treasury to be applied to the state's outstanding loan balance. Due to amended returns, the state occasionally still receives some funding due to this 2010 tax increase.

¹⁷ Account Statement June 2015: http://www.treasurydirect.gov/govt/reports/tfmp/tfmp_utf.htm

Figure 5: UI Trust Fund Balance as of June 30th, 2002-2015



Conclusion

FY2015 was an important year for the South Carolina Unemployment Insurance Trust Fund. On June 11, 2015 the final federal loans taken during the Great Recession to pay benefits were repaid. This repayment was in accordance with the five-year plan adopted by the General Assembly in 2010. Tax year 2016 will be the beginning of another five-year plan to build the Trust Fund to a level that is considered adequate to withstand a moderate recession. Benefit payments continue to remain at historic lows as the state's economy has continued to recover and expand.