

Campaign to Reduce Child Poverty

Policy Brief #8

STRENGTHENING THE NEW MEXICO ECONOMY THROUGH UNEMPLOYMENT INSURANCE REFORM

Introduction

In August of 2002, New Mexico's seasonally adjusted unemployment rate was 6.1%, down slightly from the previous month's rate of 6.3%, and a substantial increase over the 4.7% rate of August 2001. New Mexico's unemployment rates for 2002 are the highest since 1998, but lower than those of the eighties and early nineties, when unemployment often exceeded 7% (NMDOL, 2002). Nationally, unemployment averaged 5.7% in August. Eight states had unemployment rates higher than New Mexico's.

This year's federal economic stimulus bill transferred \$8 billion from the federal unemployment insurance trust fund to state unemployment insurance trust funds in what is known as a Reed Act distribution. New Mexico's share of the 2002 Reed Act distribution totaled \$39 million. Reed Act funds can be used to finance unemployment insurance (UI) eligibility expansions and increase UI benefit levels. Reed Act money can also be used by state UI offices to hire additional personnel and implement new technologies needed to carry out UI reform. But before the Reed Act money can be put to any constructive use, legislation to appropriate it must be enacted.

Unemployment Insurance Bolsters the Economy

Unemployment insurance is the first line of defense protecting workers, families, and communities during an economic downturn. A second, but equally important function of unemployment insurance is to stimulate the economy and protect small business during recession by putting money in the pockets of people who are very likely to spend it. The US Department of Labor estimates that during economic slowdowns each \$1 spent on unemployment insurance generates \$2.15 in gross domestic product.

A robust unemployment insurance system is essential to the health and stability of working families and the communities in which they live. Fortunately, unlike the unemployment insurance systems of many other states, New Mexico's unemployment insurance system has more than adequate funds with which to pay benefits and New Mexico could easily afford to both expand eligibility and increase benefit levels.

The ***unemployment trust fund*** is the amount available for payment of unemployment insurance benefits. In July of 2002, the New Mexico trust fund balance was \$585.8 million. UI benefits are financed through state payroll taxes paid from state trust funds maintained at the US Treasury. Despite recession, New Mexico's trust fund remains the nation's most solvent. **Existing reserves are adequate to pay benefits for almost 3 recessionary years without any additional revenue. The national average is about one year.**

Most unemployed workers in New Mexico don't get UI. Nationwide, 43.3% of unemployed workers receive unemployment insurance benefits. In New Mexico the UI participation rate is much lower - only 28.8% of workers who become unemployed and are actively seeking other work are eligible for unemployment insurance. New Mexico ranks 41st among states in the percent of unemployed workers who qualify for UI (Emsellem et al, 2002).

Barriers to UI

One reason New Mexico's UI trust fund balance is so high is that while 99% of New Mexico employers pay into the trust fund on behalf of their employees, fewer than one third of unemployed New Mexicans are actually eligible for unemployment insurance. This is because state laws governing unemployment insurance eligibility and benefits have not kept pace with the changing characteristics of New Mexico's workforce. For example, an increasing percentage of New Mexico's workers are women, many of whom work part-time or part-year in order to juggle responsibilities at home.

According to the 2000 US Census, 55.4% of New Mexico children under 6 live in families in which both parents work. Full-time center-based infant care costs around \$550 a month, or over half the gross income of a full time minimum wage worker. Many parents of small children have no choice but to accommodate their work schedules to the availability of relatives or neighbors willing to provide affordable child care. If an unemployed parent turns down a full-time job offer because the work schedule is incompatible with their child care schedule, the parent may be denied UI.

New Mexico's economy continues to rely heavily on low-paying service sector jobs and work requirements imposed as part of welfare reform have further increased the number of low wage and low skill workers.

Eligibility for unemployment insurance is restricted to workers terminated from their jobs through no fault of their own. Workers who are fired or quit can only collect UI if it is determined that they were not fired for misconduct or if they can prove that they quit because of a work-related problem that was caused by their employer.

In New Mexico, workers who are forced to leave their job by circumstances that are not related to employment, such as domestic violence, loss of child care, or the illness of a family member, are not eligible for UI. Lack of protection for these workers is disproportionately damaging to women because women are more likely to be victims of domestic violence and the primary caregivers for children and other dependent relatives.

Seventeen states have laws that specifically allow workers who leave their jobs because of domestic violence to collect UI. Fifteen states allow workers who leave their jobs for certain "domestic reasons," such as caring for ill, injured, elderly, or disabled family members, to collect UI. California and Arizona are among states that extend UI eligibility to parents who "voluntarily" quit because they can no longer obtain child care (Foster, 1998). The growing number of women in the workforce are particularly vulnerable to UI denial because of these exclusions.

Workers must meet minimum earnings requirements to qualify for UI. In general, a worker paid the federal minimum wage of \$5.15 an hour must have worked at least 20 hours a week to qualify for UI. Someone paid the state minimum wage of \$4.25 per hour must have worked at least 24 hours per week.

New Mexico is one of 30 states that require UI beneficiaries to actively seek work that is “substantially full time” regardless of their work history, occupation, or other constraints on the amount of time they are available to work. Roughly 15% of New Mexicans work part-time and most part-time workers are women (Emsellem et al, 2002). People seeking part time work are ineligible for unemployment insurance even if their previous employment was part time and they have compelling reasons, such as child care obligations, for seeking less than full-time work¹. This provision denies UI eligibility to many workers (particularly single parents) with dependent care obligations that prevent them from working full time.

Women are less likely than men to receive unemployment insurance. Nationwide, 45.9% of men receive UI, compared to 40.0% of women. In New Mexico, 26.3% of unemployed women receive UI compared to 30.8% of men (Emsellem et al, 2002). Denying eligibility to part-time workers widens the UI gender gap, because over two-thirds of part-time workers are women.

In New Mexico, as in most states, UI claims are based on wages earned in the first four of the previous five calendar quarters of work². This is known as the base period. Benefits are never based on wages in the three months immediately prior to filing the claim. The base period method of determining UI eligibility and benefits currently utilized in New Mexico was instituted before the use of computers made it possible to verify UI claims using information from the most recent quarter of work.

New Mexico’s base period method of determining eligibility and benefit levels penalizes workers who have limited or interrupted work histories, most notably seasonal workers, temporary workers, recent graduates and other people new to the labor force, including workers transitioning off welfare. Advances in technology have made verification of

UI claims faster and more efficient. As a result, many states have begun adopting “alternate” base periods that include a worker’s most recent earnings in determining eligibility and benefit levels.

Strict UI eligibility rules combined with time limits on welfare benefits make parents transitioning off welfare and into the labor force particularly vulnerable to hardship if they are laid off. Prior to the 1996 welfare reform law, welfare provided a second-tier safety net for unemployed single parents who were ineligible for UI. Unfortunately, most workers new to the labor force, especially low-wage workers who may have a hard time meeting minimum earnings requirements, and those working part-time, are ineligible for UI. Thus, workers who have reached the time limit on welfare benefits and lose their job may be unable to access any form of income support for themselves or their families.

Limited eligibility for UI may undermine the effectiveness of welfare-to-work programs because former welfare recipients who have not yet reached their time limit on benefits and do not qualify for UI may find they have no choice but to return to welfare if they lose their jobs.

Benefits

Low benefit payments are another reason for New Mexico’s large unemployment insurance system surpluses. In New Mexico, UI recipients receive a benefit equal to one-half of their average weekly earnings *if* their average weekly earnings were less than 1.05 times the average weekly wage for the state. As of January 2002, the average wage in New Mexico was \$14.03 per hour, or about \$560 per week. For workers whose earnings are more than 6% above the state average weekly wage, benefits are capped at 52.5% of the state average weekly wage, or about \$277 per week. Maximum weekly UI benefits range from \$190 in Alabama to \$496 in Washington state. **Thirty-eight states provide a higher maximum benefit than New Mexico’s.**

New Mexico's average weekly UI benefit as of June 2002 was \$201, slightly over one third of the average weekly wage, and 30% **below** the poverty threshold for a family of three. For a minimum wage worker the weekly benefit amount was \$103 - 64% below the poverty threshold for a family of three. Nationally, almost one-third of unemployed workers don't have enough savings to replace even 10% of the wages lost during a period of unemployment (Gruber, 2002). For these workers, a period of unemployment can mean incurring crushing debt, going onto welfare, or doing without necessities like utilities, clothing, or food.

UI benefits are based on prior wages and are thus not a direct function of need. While few households can survive on an income less than half of their working wage for long, the deprivation associated with spells of unemployment may be particularly severe for families with children, non-working spouses, and elderly or disabled dependents. Thirteen states have enacted a UI "**dependent allowance**" which augments UI benefits by a set amount per dependent. Massachusetts, for instance, pays UI beneficiaries an additional \$25 per dependent per week. Some states have variable dependent allowances. Ohio's dependent allowance ranges from \$1 to \$88 per dependent per week. All states that have dependent allowances count unmarried children under 18 as dependents for purposes of UI. Most also count non-working husbands or wives. Michigan, Iowa, and Washington DC allow dependent allowances for disabled parents and siblings of workers receiving UI. In 2001, approximately 52% of UI claimants in New Mexico had one or more dependents.

New Mexico prohibits workers from receiving unemployment benefits for their first week of unemployment. This provision effectively reduces benefits by one week for the two-thirds of unemployed workers who don't exhaust their UI benefits. Seventeen states do not require a "**waiting week**."

Especially during recession, many workers exhaust their UI benefits before they are able to find another job. In June 2002, 35% of workers

receiving UI in New Mexico exhausted their benefits, compared to 30.2% in June of 2001. Regular unemployment benefits last for 26 weeks and are paid entirely out of state trust funds. Current law allows for 13 additional weeks of benefits (known as "extended benefits") in times of high and increasing unemployment. The cost of paying extended benefits is divided equally between the states and the federal government.

Under current New Mexico law, extended benefits "trigger" when the percent of the labor force that is unemployed *and* receiving UI benefits, called the **insured unemployment rate**,³ exceeds 5% and unemployment is 20% higher than it was in the same 13 week period in each of the previous two calendar years or when the insured unemployment rate exceeds 6%. Due to New Mexico's low rate of UI participation, the insured unemployment rate is a highly inaccurate gauge of economic hardship. In August, the insured unemployment rate was 1.9%, while the actual unemployment rate was 6.1%. Extended benefits last triggered in New Mexico in 1982, when the total unemployment rate was 9.2%.

Although extended benefits are administered in partnership with the federal government, states have some discretion in setting their extended benefits trigger and determining the length of time for which extended benefits are paid. For instance, states can opt to allow extended benefits to trigger when **total** unemployment exceeds 6.5%.

UI Taxes

Unemployment benefits are financed through state payroll taxes paid from state trust funds maintained at the US Treasury⁴. Employers pay 100% of UI taxes. They are prohibited by law from passing UI taxes on to employees as explicit payroll deductions. However, research indicates that most of the burden of the UI tax is nonetheless borne by workers in the form of lower wages (Gruber, 1997). Ninety-nine percent of New Mexico

employers either pay the UI tax or reimburse the state for benefits paid to their employees⁵.

The New Mexico Department of Labor tracks employer deposits and withdrawals from the UI trust fund using a system of individual employer “accounts.” Employer accounts are credited with tax payments and charged with benefits paid to former employees based on the wages reported under that account. The extent to which tax payments exceed benefits charged is the employer’s “*account balance*.” The account balance divided by the average annual payroll for the three preceding fiscal years is an employer’s “*reserve ratio*.” Employers are assigned a UI tax rate for each calendar year based on their reserve ratio. This is known as “*experience rating*”. The lower the reserve ratio the higher the tax rate.

Currently, New Mexico unemployment insurance tax rates range from .05% to 5.4%. **Over 40% of New Mexico employers pay the lowest UI tax rate of .05%, or about \$8 per employee per year.**

Tax rates are also a function of state trust fund balances. Trust fund balances determine the schedule used in assigning tax rates. When trust fund balances are high relative to the state’s total annual payrolls, a schedule with lower rates is employed. Currently, New Mexico is using the lowest schedule. In New Mexico taxable payrolls for calendar year 2001 totaled \$15,179,133,000.

Table 1 provides tax rates by employer reserve ratio and rate schedule. Currently, schedule 1, the schedule with the lowest tax rates, is being utilized. Schedule 1, which is highlighted, is used if the ratio of the trust fund to total payrolls exceeds 3.39%. At present, the ratio of the unemployment trust fund to total payrolls is approximately 3.9%.

Table 2 gives the ratio of trust fund to total annual payrolls associated with each rate schedule. Line 3 (lighter shading) of table 2 gives the minimum trust fund balance necessary to

UNEMPLOYMENT INSURANCE TAX RATE SCHEDULE						
	SCHEDULE					
	1	2	3	4	5	6
RESERVE RATIO						
10% or greater	0.05%	0.1%	0.6%	0.9%	1.2%	2.7%
9.0 to 9.9%	0.1%	0.2%	0.9%	1.2%	1.5%	2.7%
8.0 to 8.9%	0.2%	0.4%	1.2%	1.5%	1.8%	2.7%
7.0 to 7.9%	0.4%	.6%	1.5%	1.8%	2.1%	2.7%
6.0 to 6.9%	.6%	.8%	1.8%	2.1%	2.4%	2.7%
5.0 to 5.9%	.8%	1.1%	2.1%	2.4%	2.7%	3.0%
4.0 to 4.9%	1.1%	1.4%	2.4%	2.7%	3.0%	3.3%
3.0 to 3.9%	1.4%	1.7%	2.7%	3.0%	3.3%	3.6%
2.0 to 2.9%	1.7%	2.0%	3.0%	3.3%	3.6%	3.9%
1.0 to 1.9%	2.0%	2.4%	3.3%	3.6%	3.9%	4.2%
.9 to 0.0%	2.4%	3.3%	3.6%	3.9%	4.2%	4.5%
-.1 to -.5%	3.3%	3.6%	3.9%	4.2%	4.5%	4.8%
-.6% to -1.0%	4.2%	4.2%	4.2%	4.5%	4.8%	5.1%
-1.1% to -2.0%	5.0%	5.0%	5.0%	5.0%	5.1%	5.3%
Under -2.0%	5.4%	5.4%	5.4%	5.4%	5.4%	5.4%

maintain each rate schedule given New Mexico’s 2001 annual payroll estimate. Line 4 (darker shading) gives the amount by which the current trust fund balance could be drawn down before triggering a shift in the rate schedule.

Tax Rate Schedule	1	2	3	4	5	6
UI trust fund as a percentage of total payrolls	>3.39%	2.7%-3.39%	2%-2.69%	1.5%-1.99%	1%-1.49%	<1%
Minimum trust fund balance necessary to maintain these rates*	\$516,090,522	\$409,836,591	\$303,582,660	\$227,686,995	\$151,791,330	n/a
Amt by which current balance could be drawn down without schedule change	\$80,709,478	\$186,963,409	\$293,217,340	\$369,113,005	\$445,008,670	n/a

* Assumes calendar year 2001 total payrolls of \$15,179,133,000 Source: US Department of Labor, Employment and Training Division, Workforce Security Division.

The **taxable wage base** is the amount of employee wages upon which an employer pays UI taxes. Employers pay UI taxes on all of an employee's wages up to the taxable wage base, regardless of how much the employee works. In New Mexico, the taxable wage base is indexed to the average state wage. For 2001, the taxable wage base in NM was \$15,200. The taxable wage base for 2002 is \$15,900.

UI tax rates in New Mexico currently average 1.2% of taxable wages and .6% of total wages per employee. A typical employer, paying the average tax rate will pay UI taxes of approximately \$124 per worker per year for full time minimum wage workers and \$191 per worker per year for all full time workers making over \$7.60/hour.

Like all taxes levied on employers, UI taxes have the potential to hamper business investment and stifle job growth, *if* they are set too high. Workers, however, are the backbone of the economy and it is incumbent upon employers to do their part to ensure that workers who lose their jobs through no fault of their own survive economically while looking for other work.

The UI system must therefore balance the interests of workers against the interests of employers, recognizing that the two are not always mutually exclusive. Employers benefit from the UI system through reduced turnover – workers who are not forced by financial necessity to take the first job they find are less likely to quit once they become employed. More importantly, UI helps sustain the local economy when the workers who

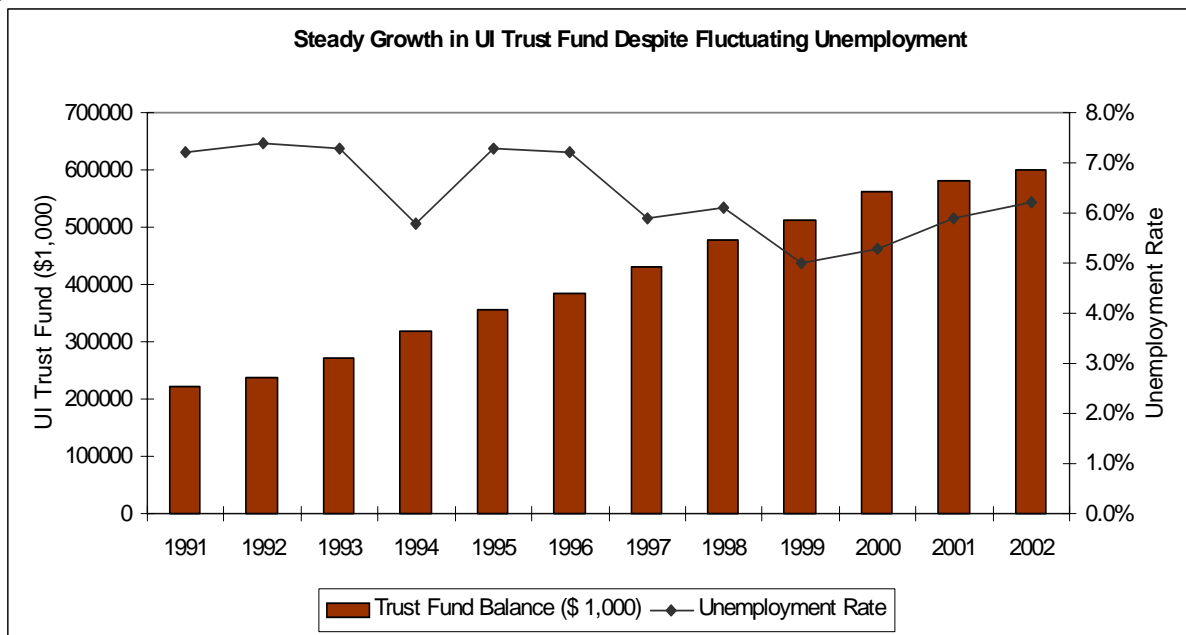
patronize local businesses lose their jobs. Workers benefit when the tax burden on business is minimized because payroll taxes, even when they are paid by employers, are passed on to workers in the form of lower wages.

Fortunately, the UI tax burden in New Mexico is quite modest. In addition, as mentioned earlier, the New Mexico UI trust fund is extremely robust. The solvency of state UI trust funds is measured by their **average high cost multiple** (AHCM). The AHCM is the number of years a trust fund can pay UI benefits at average recessionary levels *without taking in any additional revenue*. New Mexico has the nation's most solvent UI trust fund. New Mexico's trust fund could pay UI benefits at recessionary levels for two years and eight months without taking in any UI taxes, longer than any other state.

Proposed reforms

New Mexico is in an excellent position to enact UI reforms. We have the need - New Mexico has a higher-than-average unemployment rate and one of nation's lowest UI utilization rates - and we have the ability, New Mexico's UI trust fund is the nation's most solvent. The following reforms are needed to correct overly strict eligibility requirements and inadequate benefits:

- ✓ **Adopt an "alternative base period"** that uses the most recent calendar quarter of work to establish a UI claim if a worker does not qualify for UI using the regular



- base year. Adopting a base period that includes a worker's most recent earnings in determining eligibility and benefit levels would increase the number of low income New Mexico workers who are eligible for UI. Twelve states have already adopted an alternative base period.
- ✓ **Cover workers who "voluntarily" leave their jobs for "compelling domestic reasons"** including child care conflicts, domestic violence, and sick dependents and **exempt employers from penalty** for those employees who qualify for UI based on domestic circumstances. The UI tax rate an employer pays is determined, in part, by the amount of UI benefits paid to his former employees. Employers should not be penalized with higher tax rates if their employees collect UI after quitting or being discharged for compelling domestic reasons.
 - ✓ **Eliminate the one-week waiting period** for UI benefits. It imposes unnecessary hardship on unemployed workers and their families and serves no administrative purpose.
 - ✓ **Adopt average benefit amounts that exceed the federal poverty level.** A weekly wage of \$289 places a family of three at the federal poverty threshold. The current average UI benefit in New Mexico is \$201.
 - ✓ **Enact a "dependents allowance" of \$15 per week per dependent.** A single person with no dependents making \$200 per week is not poor, whereas a family of three trying to live on the same amount is. An incremental increase in UI benefits based on the number of dependents a worker has would improve the ability of the UI system to sustain families through periods of unemployment.
 - ✓ **Make extended benefits more readily available during recession by adopting a 6.5% total unemployment extended benefits trigger.**
 - ✓ **Cover workers who previously worked part-time and are seeking part-time work.**

Conclusion

Unemployment insurance can be a crucial safety net for working families and a powerful antidote to recession, *if* it is administered properly and with these goals in mind. A well-functioning system balances the needs of workers against those of employers, providing adequate protection to workers during spells of unemployment at the lowest possible cost to employers. New Mexico's current UI system functions poorly because the criteria governing UI eligibility and benefits are outdated. New Mexico currently has the nation's most solvent UI trust fund, competitive employer tax rates, and the ninth lowest rate of UI utilization. Reforming New Mexico's unemployment insurance system strengthens our labor force, sustains communities, and bolsters local business in hard economic times.

¹ The cost of full-time center-based infant care averages about \$550 per month in Albuquerque, making full-time minimum wage employment economically unfeasible for many parents.

² To be eligible for benefits, a worker must have had wages in two different quarters of the 12-month period immediately preceding the quarter in which they lost their job.

³ The insured unemployment rate does not account for workers who have exhausted their UI benefits. It also does not include unemployed workers from industries not covered by state UI laws, the self-employed, unpaid family workers, and some agricultural workers. The insured unemployment rate also does not include unemployed Federal workers, members of the Armed Forces, railroad workers, and workers of some nonprofit organizations (Moskowitz, 2001).

⁴ There is also a federal UI tax (levied on the first \$7,000 in income at a rate of .8%, for a maximum of \$56 per worker per year) that pays the costs of administering the state and federal trust funds and finances Extended Benefits (EB) during periods of high unemployment.

⁵ Ninety four percent of New Mexico employers are subject to UI tax. Another 5% reimburse the state for benefits paid to their employees. One percent of employers do not participate in the UI system.

Sources

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