

THE NEED TO STRENGTHEN NEW MEXICO'S UNEMPLOYMENT INSURANCE TRUST FUND

May 2012

INTRODUCTION

At no point in history since the end of the Great Depression has the unemployment insurance program been more important to New Mexico's displaced workers than it has over the last few years. Since late 2007, New Mexico has been experiencing a dramatic business cycle—one that has not been common in the state's recent economic history. In the two national recessions before the Great Recession (those in 1990-91 and 2000-01), New Mexico employment was relatively unscathed. In part, this was because New Mexico did not appreciably enjoy the employment booms in the preceding bubbles. In the Great Recession that started in December 2007, this was not so—New Mexico workers have had a very rocky time of it. The housing bubble that was at the heart of the 2007 downturn had been good for New Mexico workers—particularly those in the construction industry and other job sectors that benefited from robust real estate sales.

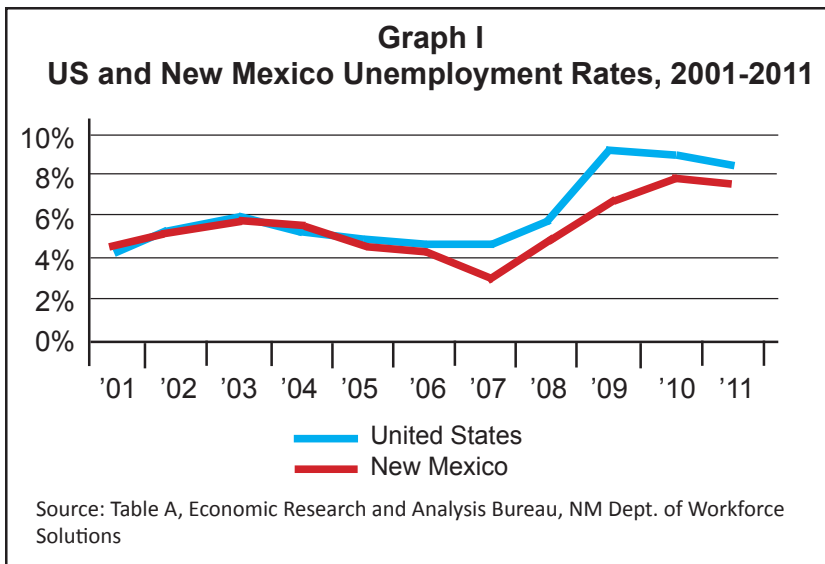
Programs like unemployment insurance (UI) act as a counter balance when unemployment rises and the economy goes south. They help keep consumer spending

up while helping families pay their bills and put food on the table. UI payments to the newly unemployed had begun to rise in early 2008 and continued through 2011. As is typical, the balance of the UI Trust Fund—the 'savings account' in which UI funds are kept—began to decline. Normally, payments into the fund—made by employers—also rise automatically in New Mexico to keep pace with benefits paid out. In 2010, however, due in part to changes put in place by state lawmakers, payments into the fund dropped off precipitously.

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In 2011, UI benefits to students and displaced workers with dependent children were decreased. In effect, rate cuts for businesses were provided on the backs of the unemployed and their children. This would be unfair to do during a healthy economy. It is unconscionable to do during a recession. As a result of a particularly deep

recession and employer rate cuts, New Mexico's UI Trust Fund is not healthy and is not likely to regain its fiscal health before the next recession, when it will again be stressed by economic pressures.



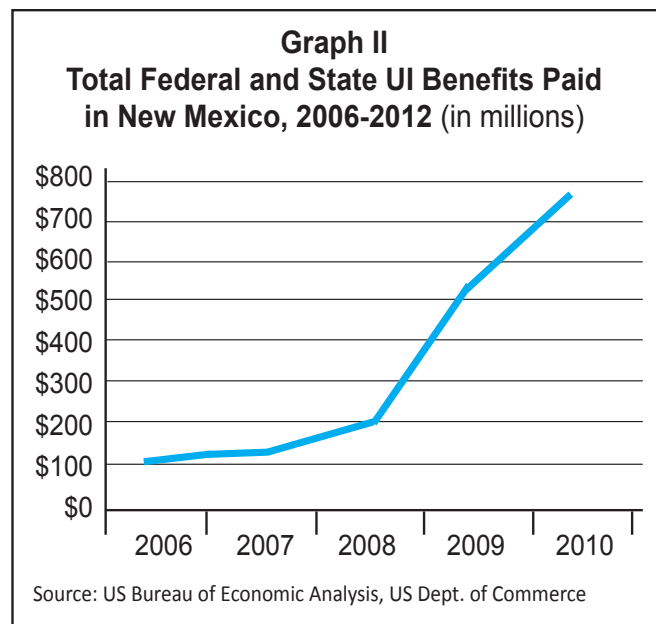
FALLING EMPLOYMENT; RISING UI PAYMENTS

As Graph I (*US and New Mexico Unemployment Rates, 2001-2011*, above) shows, New Mexico’s unemployment rate fell as low as 3.5 percent in 2007 at the height of the state’s housing construction boom. After the bubble deflated, the unemployment rate ratcheted up to 8 percent at the worst point of the recession (the third quarter of 2010). By January of 2012, as the recovery took hold, New Mexico’s seasonally adjusted unemployment rate had subsided to 7 percent.

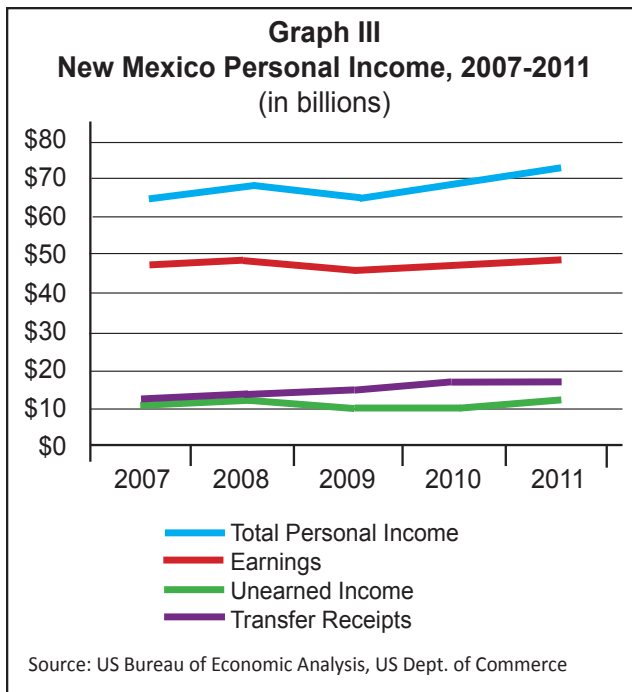
New Mexico’s unemployment insurance (UI) system carried out its primary function during the economic downturn that started in late 2007—the function of maintaining purchasing power in the economy when consumer spending is falling due to rising unemployment. Economists call unemployment insurance a ‘counter-cyclical’ program, meaning that it counteracts the effects of an economic downturn by helping to keep consumer spending from falling, which would make the economy worse. The loss of income associated with rising unemployment directly causes a decline in consumer spending and, indirectly, a decline in investor spending because machinery needed for producing consumer goods is also not needed. Unemployment insurance spending stimulates

the economy because it is not directly funded by taxes—money that had already been circulating in the economy. That is because the source of benefits payments is in effect a savings account—the UI Trust Fund. During the recession, the savings from the UI Trust Fund are spent in the form of UI benefits paid to people who have lost their jobs. The Fund usually collects more than it pays during a robust economy and then pays out more than it receives during a downturn.

Graph II (*Total Federal and State UI Benefits Paid in New Mexico, 2006-2012*, below) illustrates the sharp increase in UI payments beginning in 2008.



‘Personal income’ is a measure used by economists to describe a state’s economy. Graph III (*New Mexico Personal Income, 2007-2011*, page 3) shows the behavior of personal income before and during the financial crisis that followed the collapse of the housing bubble. New Mexico personal income fell between 2008 and 2009, which is extremely unusual.

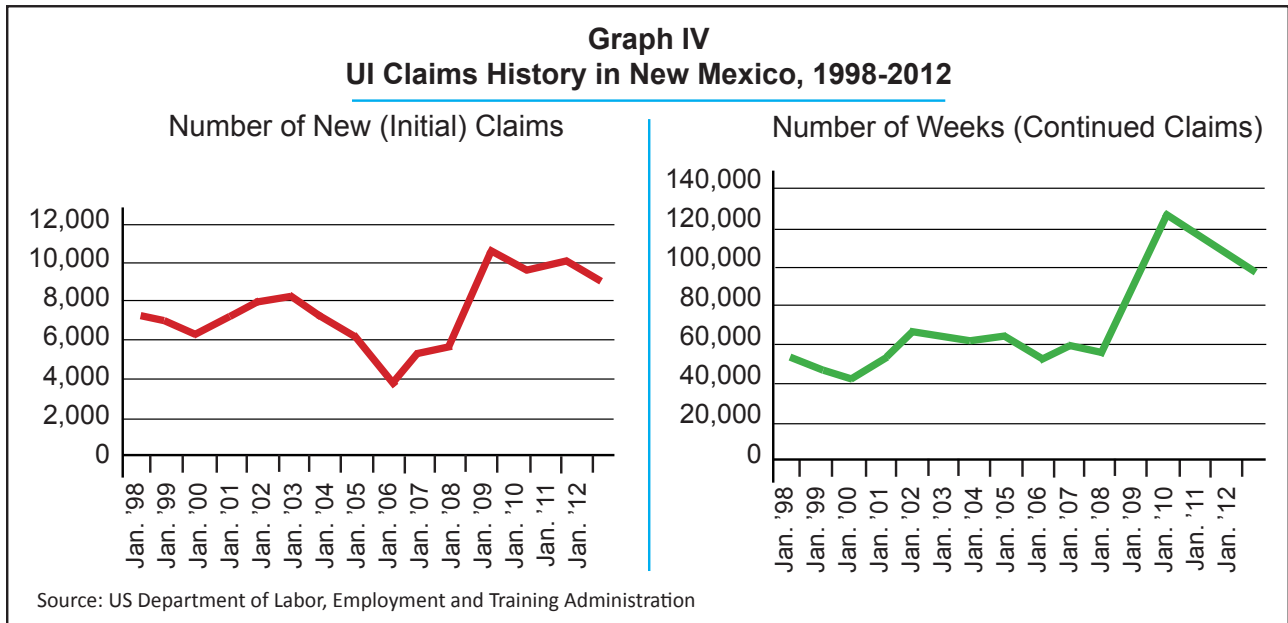


As both earnings and unearned income (dividends, interest, and rent) fell, transfer receipts (payments such as UI and Social Security, Medicaid and Medicare benefits, and other assistance programs such as SNAP/food stamps) rose to take up some of the slack. But the graph indicates that transfer receipts, which are designed to rise more sharply during a crisis, failed to respond quickly enough to prevent a fall in personal income in the early part of the recession.

By 2010, substantial growth in transfer payments, combined with some growth in total income, was having the desired effect on the state's economy. Total transfer receipts (including Social Security and medical benefits) went up by 50 percent between 2006 and 2010. The growth in UI payments was almost 700 percent, making it a much larger share of total transfer payments.

Graph IV (*UI Claims History in New Mexico, 1998-2012*, below) shows the rise and fall of initial claims (the measure of new claims) and continued claims (the measure of weeks UI benefits are claimed). Initial claims (the red line in Graph IV) were on pace with the unemployment rate from 2000 to 2012. Initial claims had peaked in 2003 from the so-called dot-com recession. As the housing construction boom took hold, initial claims for UI fell in 2006 then began to climb in January of 2007, finally doubling by January 2009. Initial claims fell in January 2012—a sign that the recovery was clearly taking hold.

While initial claims peaked in January 2009, continued claims (the green line in Graph IV) did not peak until January 2010. This indicates that it took longer for the unemployed to find jobs during the Great Recession than it did during the 2000-01 recession caused by

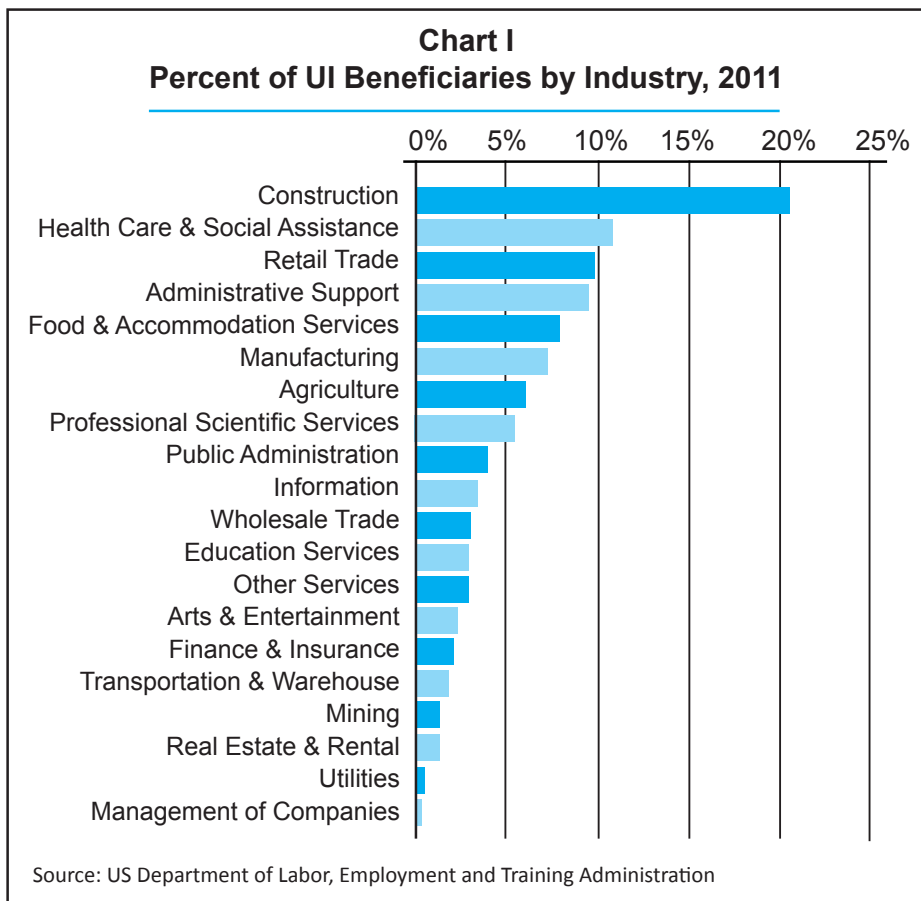
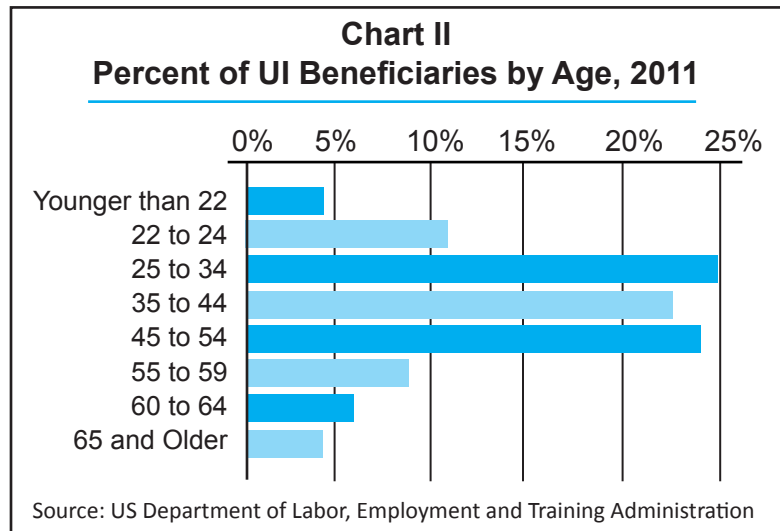


the collapse of the so-called dot-com bubble. This is a sign of an anemic recovery.

CHARACTERISTICS OF NEW MEXICO'S UI BENEFICIARIES

When considering the UI system, it is helpful to look at some of the demographic characteristics of its beneficiaries. This also gives us a more complete picture of how the Great Recession has impacted New Mexico workers—particularly those with families. Chart I (*Percent of UI Beneficiaries by Industry, 2011*, below) shows plainly how the construction industry took the brunt of the job losses following the bursting of the housing bubble. The pre-recession growth in construction jobs—the result of a housing construction binge—was unsustainable.

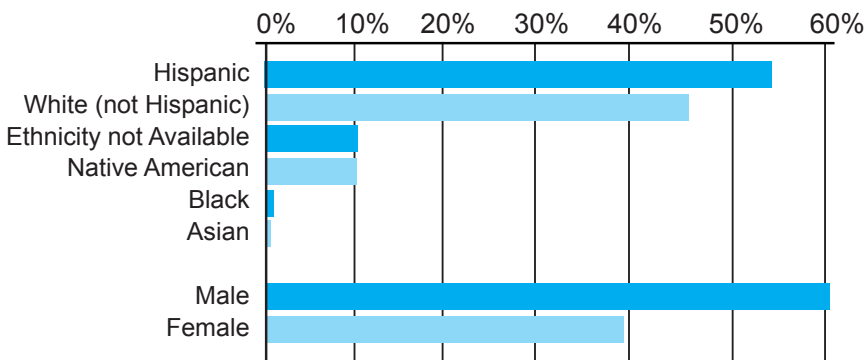
Former construction workers represented the largest share of UI beneficiaries, followed by unemployed workers from the health care and education sectors (which the US Department of Labor groups together as 'health care and social assistance,' as shown in Chart I). A significant share of UI beneficiaries



could also be found in retail trade, manufacturing, and administrative support.

As construction workers are overwhelmingly young men—and in New Mexico, also Hispanic—the next two charts show a correlation with Chart I. As Chart II (*Percent of UI Beneficiaries by Age, 2011*, above) indicates, the largest percentage of UI beneficiaries fell in the 25–34 age group—the age group most likely to have young children. Those between 35 and 54—considered the prime earning years—were also greatly impacted by job losses.

Chart III
Percent of UI Beneficiaries by Race/Ethnicity* and Gender, 2011



*Total exceeds 100 percent due to overlap in reporting
 Source: US Department of Labor, Employment and Training Administration

Americans, Blacks, and Asians were UI beneficiaries is most likely due to the fact that they are not employed in large numbers in the sectors that had the highest job losses.

Finally, men were about 60 percent of UI beneficiaries while women were 40 percent.

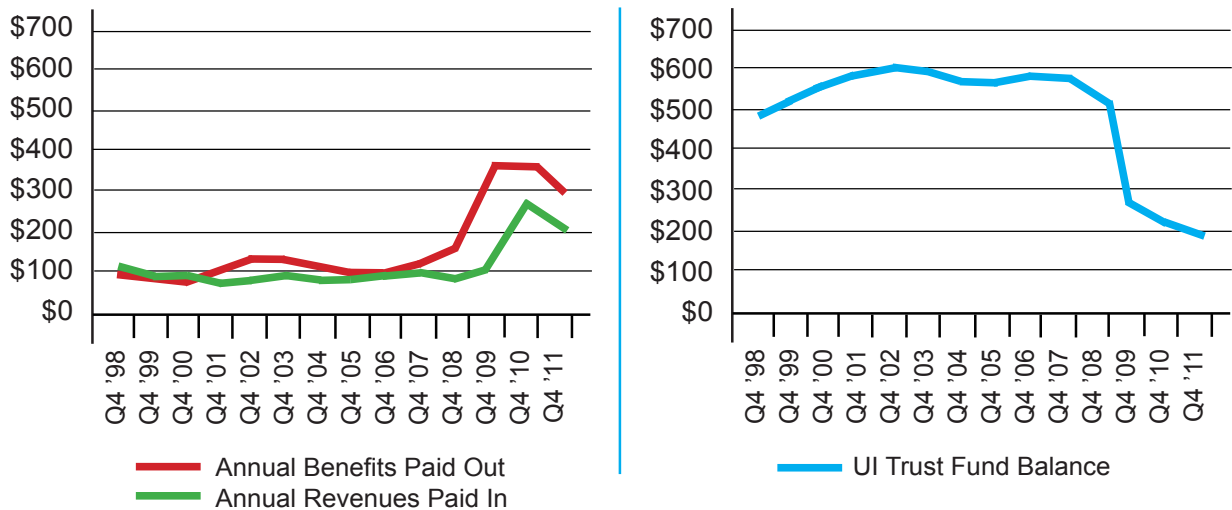
A TROUBLED TRUST FUND

The balance of the UI Trust Fund, which is held by the US Department of Labor, is the

More than half of the insured unemployed were Hispanic (see Chart III, *Percent of UI Beneficiaries by Race/Ethnicity and Gender, 2011*, above) and non-Hispanic Whites were about 42 percent. Because of their prevalence in the construction industry, Hispanics were not only disproportionately impacted by job losses, but also disproportionately assisted by the UI program. That smaller percentages of Native

amount available for payment of UI benefits. The UI program takes in revenues in the form of levies on employers and spends the revenues as benefits for qualifying dislocated workers. Although UI claims payments have slowed since the peak of the recession, benefits paid for both initial and continued claims are still exceeding revenues from employer premiums. As illustrated in Graph V (*New Mexico UI Trust Fund*

Graph V
New Mexico UI Trust Fund History, 1998-2011 (in millions)



Source: US Department of Labor, Employment and Training Administration

History, 1998-2011, page 5), starting in the fourth quarter of 2008 (Q4 '08) benefits paid (the red line) far exceeded revenues received (green line). This kind of depletion of the UI Trust Fund is expected during a recession, although the depth of the Great Recession in New Mexico was not expected by experts on the state's economy. However, as benefit payments decline, the balance (blue line) should begin to recover. Graph V shows that it most clearly is not happening.

In 2003, the state Legislature made several changes to the UI system, including increased benefits for bread-winners with dependent children and a lower insurance rate for employers. (For a more complete history of changes to New Mexico's UI system from 2003 to the present, see the Appendix, page 7.) Since employer payments are a percentage of their payroll, they decline during a recession as workers are laid off. To counteract that—and to keep the Trust Fund solvent—New Mexico's UI statute has a built-in method for increasing premiums when wages fall. These automatic increases, which would have helped keep the UI Trust Fund balance from dropping so dangerously low, were overridden by the Legislature during the entire 2003-2012 period.

CONCLUSION

There is a need for action on rebuilding the UI Trust Fund as the recovery from the recession continues so it will be available when the next recession—and its ensuing wave of unemployment—hits. The solution to the depletion of the UI Trust Fund is to increase employer contributions, not to cut UI benefits. Cuts to benefits during a recession hurt more than the workers and their families. They also slow the recovery, which impacts everyone—employers included. Had the UI statute's method for increasing employer payments been kept in place, the fund would not be in such a dire condition. State lawmakers should allow the statute to work as it was intended so employer rates can return to where they should be at this point in the recovery.

LINKS TO SOURCES

US Bureau of Economic Analysis, US Department of Commerce:

<http://bea.gov/iTable/iTable.cfm?ReqID=70&step=1&isuri=1&acrdn=3>

US Department of Labor, Employment and Training Administration:

<http://workforcesecurity.doleta.gov/unemploy/content/data.asp>

APPENDIX

An Abridged History of Legislative Changes to the New Mexico Unemployment Insurance Program Since 2003

INTRODUCTION

Section 51-1-11 NMSA 1978 is the statute defining six schedules for determining employer contributions. These are based on the size of the UI Trust Fund as a percentage of the state's total payroll. The larger the Trust Fund is as a percentage of total payroll, the lower the employer contributions are. The schedules range from 2.3 percent of total payroll (Schedule 0) to 0.3 percent (Schedule 6).

2003 – With the UI Trust Fund balance at \$588 million and unemployment at 5.9 percent, the Legislature implements several changes to the UI system. Some of them benefit the unemployed and some the employers:

- A trigger is put in place that would automatically extend benefits when total unemployment reaches a certain level;
- Benefit payments are increased from 50 percent of high-quarter wages to 52.5 percent;
- A dependent allowance of \$15 weekly per dependent is added;
- It is determined that separation from employment as the result of domestic violence constitutes a valid reason for claiming UI benefits;
- Automatic benefit denial for students attending school full-time is eliminated;
- An 'Alternate Base Period,' which would use the most recent quarter in benefit eligibility determination, is implemented (this would have the effect of making more workers eligible for benefits);
- Benefits are allowed for claimants seeking part-time work;
- The UI tax rate for new employers is reduced from 2.7 percent to 2.0 percent; and
- A new UI employer contribution schedule (Schedule 0) with lower tax rates and a solvency trigger is implemented.

2005 – With a UI Trust Fund balance of \$559 million and an unemployment rate of 5.2 percent:

- The 2003 reforms are suspended because of the "extremely tight" trigger mechanism; and
- The trigger rate is dropped from a UI Trust Fund balance of 3.75 percent of total payroll to 2.5 percent of total state payroll.

2006 – With a UI Trust Fund balance of \$578 million and an unemployment rate of 4.1 percent:

- UI tax Schedule 0 is put into effect for employers with a reserve ratio of 15 percent or higher. Legislative Council Services determines in its fiscal impact report that this will have no detrimental fiscal impact.

2007 – With a UI Trust Fund balance of \$575 million and an unemployment rate at a low 3.5 percent, the 2003 set of benefit enhancements are made permanent and some are increased:

- The weekly benefit amount is increased from 52.5 percent to 53.5 percent of average weekly wage; and
- The dependent allowance is increased from \$15 to \$25 weekly per dependent with a maximum of four dependents.

2009 – With a falling UI Trust Fund balance of \$281 million and a rising unemployment rate of 6.8 percent:

- The weekly benefit amount is increased from 53.5 percent to 60 percent for 2010 and 2011.

2010 – With a UI Trust Fund balance of \$224 million and an unemployment rate at a recession high of 7.9 percent, several measures are put in place to keep the UI Trust Fund from becoming insolvent in January 2011:

- Legislation is passed to increase the UI employer tax contribution level from Schedule 0 to Schedule 1;
- The weekly benefit amount is dropped from 60 percent back to 53.5 percent; and
- A separate UI fund for covering administrative expenses is eliminated and \$100 million of it is moved into the UI Trust Fund.

2011 – With a UI Trust Fund balance at a low \$188 million and a slowly declining unemployment rate of 7.4 percent, more measures are implemented to preserve UI Trust Fund solvency:

- Employer contribution Schedule 3 is implemented for January 2012;
- Benefits to full-time students are in effect repealed;
- The number of dependents allowed to receive the extra benefit is cut in half (from four to two);
- The state's 50 percent share of extended benefits is eliminated (meaning beneficiaries receive smaller payments).

NOTE – Governor Martinez vetoes the UI employer tax increase (the change to Schedule 3) but allows the benefits reduction to stand. A suit is filed and the New Mexico Supreme Court finds that the Governor's veto of the tax increase portion of the bill is unconstitutional. Schedule 3 is still set to be in effect in 2012.

2012 – While New Mexico's UI Trust Fund is still at risk of depletion and job growth still anemic (actual numbers are not yet available), the Legislature grants the Governor's wish to lower employer rates:

- The UI contribution is set at Schedule 2 for 2013. This will cost the UI Trust Fund \$144 million.
- After 2013, the UI employer contribution schedule will be set by section 51-1-11 NMSA 1978 (this is the statutory procedure that has been over-ridden to make ad hoc changes several times since 2003).

ALSO – A commission will be set up to recommend changes to UI employer taxes, the level of UI benefits for the unemployed, and qualifications for eligibility.

CONCLUSION

Some of the worker- and family-friendly reforms implemented over the past ten years, such as the benefit allowance, are still in effect (though reduced) and some—UI benefits for students, for instance—have been repealed. Meanwhile, employer contributions have been kept artificially low, even during the worst of the recession. This policy exacerbated the depletion of the UI Trust Fund that normally occurs during a recession. Moreover, the experience of the past ten years has shown that even a seemingly large UI Trust Fund balance (it was nearly \$600 million in 2003) can be inadequate to pay full benefits in a severe recession. Clearly, the UI Trust Fund balance should be higher—possibly as high as \$1 billion.

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