Action area 1
Adequately funding UI administration

Building Resilience:
A plan for transforming unemployment insurance

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Adequately funding UI administration

Adequate and sustainable funding for the state administration of the unemployment insurance (UI) programs is foundational to addressing the challenges and issues identified by the Government Accountability Office in their pandemic-related studies of the UI program and their designation of the program as high risk. Without an appropriate ongoing level of funding, the program will be restrained in making systemic and transformational improvements.

The federal underfunding of UI administration poses significant and far-reaching challenges to the fair and efficient operations of the UI system. The Social Security Act (SSA) authorizes grants to states for the purpose of administering their UI programs. These grants are funded by federal payroll taxes paid by employers, a portion of which are deposited in the Employment Security Administration Account for the purpose of UI administration. The amount of these funds made available for state grants is set by Congress through the discretionary budget,[45] with funding appropriated for a baseline amount of UI claims, plus a contingent amount if claims rise above the base level.

In determining the amount of appropriated funds for each state, the Department uses state-specific information that relates directly to their administrative costs. The Department of Labor (the Department) has developed a Resource Justification Model (RJM) to collect data from states and uses this data to distribute available funds accordingly.

[45] The original Social Security Act in 1935 required that all federal and state UI taxes be restricted for use by the UI program, but all UI trust funds were included with the unified budget in 1968.
For a full discussion of the history and policy issues, please see National Commission on Unemployment Compensation, *Unemployment Compensation: Final Report* (July 1980), pp. 103-104, https://books.google.com/books?id=6P7PgAxFLOkC&printsec=frontcover#v=onepage&q&f=false.

A key factor in determining state funding allocations is the amount of funding appropriated by Congress. While data compiled from states' RJM submissions outlines the total costs incurred by states to operate their programs, the Department must allocate funding based on the amount of funding *made available* through appropriations, which has been consistently less than the costs reflected in states' RJM submissions and, in many years, less than the amounts requested through the President's budget. Starting in Fiscal Year (FY) 2022, the President's Budget request was based on updates in salary rates and processing factors that had not been changed in decades, but Congress's enacted budgets have not fully reflected this increased request.

Another key challenge with the current administrative funding framework is that it is based on a state's workload, or the volume of unemployment claims. This leads to funding declines when there are improvements in the economy, and leaves states ill-equipped to respond to cyclical economic downturns, let alone an economic collapse of the magnitude experienced in spring 2020. In real terms, administrative funding declined by 23 percent between 1989 (on the eve of 1990 recession) and 2019.[46]

Generally, this erosion in funding has made it difficult for states to fill the key expert roles required to operate a UI program and to have a sufficient number of trained adjudicators, investigators, benefit payment control staff, appeals judges and claims-takers in place when unemployment rises. Additionally, funding for states is based largely on the human resources needed to process claims, despite growing use of phone and online filing. However, the outdated funding formula has not kept pace with staff costs or the costs of reinvesting in and maintaining online systems, making it difficult to support states' efficient operations of their UI systems. The funding model also does not account for investment in fraud prevention and overpayment recovery activities, such as identity (ID) verification, which are essential to program administration.

Failure to address the chronic underfunding of state UI administration will continue to challenge states' ability to improve customer service and program performance as well as effectively fight fraud. It also severely limits their ability to support continued modernization once the American Rescue Plan Act funds are depleted.

[46] Internal Department calculations.

Strategies

Completed	
1.1. Update key factors in the Department's formula for estimating state administrative funding	Historically, the only factors that changed from year to year in the formula used to determine the amount of state UI administrative funding the Department requests through the Federal budget cycle were the projected national UI workloads. However, the President's FY 2022 Budget request for state UI administration was modified to include a one-time update of the factors for workload processing productivity and state staff salary rate information, and the President's Budget has continued to request funding to support this updated formula. The factors included in the formula had not been updated in decades. Outdated measures for processing rates and salary rates resulted in estimates that were not reflective of current administrative costs. Further, the use of outdated factors contributed to states being underfunded and not being prepared for the surge in claims from the pandemic. The update of these factors resulted in an overall increase to the formula-driven budget request for state UI administrative funding.
Underway	
1.2. Evaluate the level and distribution of administrative funding	The challenges experienced by state UI programs during the pandemic have led the Department to evaluate both the level of administrative funding provided by Congress, and the mechanism used for its distribution, examining what would be sufficient funding for the operations and ongoing maintenance of state UI programs. The Chief Evaluation Office, in collaboration with the Employment and Training Administration's Office of Unemployment Insurance, is conducting a mixed methods exploratory study that aims to better understand how the costs to administer, operate, maintain, and improve state UI programs change over time and under different economic conditions. The first two phases of the study, happening concurrently, began in November 2023, and are expected to last 12 to 18 months. A third phase would answer more in-depth research questions about total funding and the RJM methodology. The findings are expected to inform potential future policy development related to UI administrative funding.

Proposed legislative reform

- **Adequately fund administrative funding –**
  Critically, core administrative funding—the amount before workload-based increases—needs to be sufficient to fund the basic administrative, technical, and legal capacities in states of all sizes. Congress should start by fully funding the President's FY 2025 Budget Request which includes updated salary and workload processing factors, and includes $25 million in funding to support the costs of ID verification in state UI programs.

- **Consider stronger, more practical enforcement levers –**
  The Department's current enforcement authority is not well structured to support the Department's UI transformation plan. Currently, the Secretary of Labor has very limited options to require state UI agencies to take actions to respond to high improper payment rates, poor performance related to the timeliness of benefits, or failure to comply with critical civil rights and access protections, and has no ability to reward states that perform well. Under the two governing statutes that regulate UI (the SSA and the Federal Unemployment Tax Act (FUTA)), the Department's only enforcement options are to withhold the state's entire administrative grant or declare employers in that state ineligible for credits against the FUTA—actions that would cause significant harm to workers and employers. Alternatives to these remedies could be authorized by law, including options for withholding a portion of a state's administrative grant and requiring states to use part of their administrative grant for specific activities to correct failed performance; or having the state participate in required technical assistance (such as a Tiger Teams assessment).

  Two additional proposals, explained in more detail under Action Area 4, Bolstering State UI Programs Against Fraud, would provide states additional resources for improving administration of UI programs. The first would allow states to retain up to five percent of recovered fraudulent UI overpayments for program integrity use. The second would require states to use penalty and interest collections solely for UI administration. Currently, states have discretion to use these funds for non-UI purposes.