

## OPEN LETTER

October 2021

Dear UI Commission Chairs Cutler and Jehlen,

In the spirit of open conversation, and to support the ongoing work of our commission, I would like to share cSPA's perspective on the most pressing needs and challenges facing the Massachusetts unemployment insurance system.

Broadly speaking, there are two issues that the state needs to address: the pandemic-driven increase in long-term liability, and our underlying structural imbalances.

*1) The increase in long-term liability from bonding our Covid-era deficit*

Unemployment insurance was a vital, and expensive, part of our response to the pandemic. It helped thousands of workers but also left Massachusetts with a multibillion-dollar UI deficit, which the state has decided to pay off over time via a bonding program.

The exact scale of the bond-related liability needs to be better understood, including updated estimates for the extent of bond issuance and the impact of any ARPA contributions. It should be relatively straightforward to provide likely scenarios, given that these estimates don't depend on future UI usage or projections of economic growth.

Uncertainties around bonding needn't impede our commission's work on addressing other issues in the UI system, since the bonds will be repaid via a separate tax.

It is important, however, to ensure that employers don't face an unreasonable *combined tax rate*, counting both the traditional UI tax and the parallel tax for bond repayment. This risk can be mitigated by taking a gradual approach to restoring solvency in the main UI system.

*2) The (in)solvency problems that have plagued the UI system for decades*

The Massachusetts UI system was underfunded well before the arrival of Covid, and it's this longer-term challenge that requires our greatest attention.

With UI, as with any state program, fiscal health depends on a balance between revenues and costs. And our UI system does have relatively high costs, even accounting for the state's high wages.\*

The main issue doesn't seem to be weekly benefit levels, as replacement rates are in line with the core expectation that benefits cover about half of lost wages. Instead, high benefit costs seem related to qualification and duration, both of which could be addressed by tackling some of the more unique features of the Massachusetts system — like the fact that roughly 10 percent of recipients collect benefits beyond 26 weeks or our openness to applicants with a limited amount of recent work.

However, while benefit adjustments may be part of the solution, revenue is the bigger challenge. In our current system, revenues automatically decline over time, continuously pushing the state toward insolvency.

Since 2004 — the last time UI tax rates were substantially changed — the effective tax rate for employers has fallen by 40 percent. On a per-worker basis, we calculate that employers have seen a 1.9 percent average tax cut every year.\*

If you go back further, you can find periods — such as 2000-02 or 1988-90 — when employer tax rates were as low as today. But those are precisely the times when solvency concerns compelled lawmakers to intervene and raise rates.

Indexing the taxable wage base is the cleanest and most effective way to end this mismatch and keep revenues balanced with benefits.

Beyond indexing the base, a decision to raise the taxable wage base would alleviate the current inequity where lower-wage (and generally smaller) businesses pay a disproportionate share of UI taxes. Ideally, the increase would be dramatic, from \$15,000 to \$40,000 or \$50,000.

To offset this large increase in the wage base, tax rates could be dramatically reduced. As a standard, rates should be set at a level that covers projected benefits and generates an annual surplus sufficient to achieve an AHCM of 1.0 within 15 years.

Moving to a system of array allocation would make it far easier to meet this actuarial goal, as it allows for year-by-year targets and a cleaner distribution of responsibility among employers.

Absent that, it's worth adding an additional rate to the top of the experience table, to cover businesses that contribute less to the UI system than their employees ultimately draw. (Massachusetts is in the top quarter of all states when it comes to the size of this mismatch.)

Finally, in terms of changing the toxic political dynamics around UI — and enabling coverage of gig workers, freelancers, and other under-protected folks — the single most important change would be the introduction of an employee tax, which would make UI feel more like Social Security: a system people pay into and can justly draw on.

To summarize, cSPA would encourage the commissioners to consider the follow approaches:

- Separate Covid-related challenges from longer-term structural issues.
- Pursue targeted benefit changes.
- Index the taxable wage base.
- Raise the taxable wage base (substantially).
- Reduce tax rates (substantially) to meet a clear actuarial standard.
- Set a relatively long-term goal for solvency, to account for the additional tax burden of bond repayment.
- Switch to array allocation.
- Introduce an employee tax.

The good news, in terms of fixing Massachusetts' UI system, is that while the rhetoric can get heated, small changes will suffice.

Unemployment insurance taxes are a tiny portion of business costs, amounting to about 1% of wages compared to 5% for Social Security — and \$600 per covered employee compared with up to \$6,000 for [health insurance coverage](#). With UI, even a 0.2 percentage point increase in effective tax rates (less, if there are benefit changes) might be enough to right the system.

It's an honor to serve on this commission and I want to personally thank you for your hard work and guidance.



Evan Horowitz  
Executive Director  
Center for State Policy Analysis  
Tisch College, Tufts University

\* You can see benefits and taxes as a share of wages [here](#), by choosing “taxable significant measures.”