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Unemployment Compensation (UC) and the Unemployment Trust Fund (UTF): Funding UC Benefits

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Summary

This report provides a summary of how Unemployment Compensation (UC) benefits are funded through the Unemployment Trust Fund (UTF). The UTF in the U.S. Treasury is designated as a trust fund for federal accounting purposes. Although the UTF is a single trust fund, it has 59 accounts: the Employment Security Administration Account (ESAA), the Extended Unemployment Compensation Account (EUCA), the Federal Unemployment Account (FUA), 53 state accounts (including District of Columbia, Puerto Rico, and the Virgin Islands), the Federal Employees Compensation Account (FECA), and two accounts related to the Railroad Retirement Board (RRB) (the RRB is discussed in CRS Report RS22350, *Railroad Retirement Board: Retirement, Survivor, Disability, Unemployment, and Sickness Benefits*. **Figure 1** depicts how transactions are required to flow through the UTF.

Federal unemployment taxes are credited to the ESAA; each state's unemployment taxes are credited to the state's unemployment account. Federal taxes pay for administration grants to the states. State unemployment taxes are dedicated to pay for regular UC benefits. The Extended Benefits (EB) program is funded 50% by the federal government and 50% by the states; however, for all states (except Puerto Rico) EB benefits are temporarily 100% federally financed by Section 4105 in the Families First Coronavirus Relief Act (FFCRA, P.L. 116-127).

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act, P.L. 116-136) created three temporary UI programs: Pandemic Unemployment Assistance (PUA), Pandemic Emergency Unemployment Compensation (PEUC), and the now-expired $600 weekly Federal Pandemic Unemployment Compensation (FPUC). The CARES Act financed these temporary UI programs using general funds of the U.S. Treasury, with the funds flowing to the states via the UTF accounts. The temporary programs were not financed through State Unemployment Tax Act (SUTA) revenue or Federal Unemployment Tax Act (FUTA) revenue and did not impact the state account balances.

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The Unemployment Compensation Program

Unemployment Compensation (UC) is a joint federal-state program financed by federal taxes under the Federal Unemployment Tax Act (FUTA) and by state payroll taxes under the State Unemployment Tax Acts (SUTA).[1] The underlying framework of the UC system is contained in the Social Security Act (SSA). Title III of the SSA authorizes grants to states for the administration of state UC laws; Title IX authorizes the various components of the federal Unemployment Trust Fund (UTF); and Title XII authorizes advances or loans to insolvent state UC programs.

Federal Unemployment Tax Act[2]

If a state UC program complies with all federal rules, the net FUTA tax rate for employers is 0.6% on the first $7,000 of each worker's earnings. The 0.6% FUTA tax funds both federal and state administrative costs as well as the federal share of the Extended Benefit (EB) program, loans to insolvent state UC accounts, and state employment services. Federal law defines which jobs a state UC program must cover for the state's employers to avoid paying the maximum FUTA tax rate (6.0%) on the first $7,000 of each employee's annual pay.

Expired Provision: FUTA Surtax

Congress first passed a temporary FUTA surtax in 1976, and since 1983 this surtax had been applied as 0.2% on the first $7,000 of employee wages until July 1, 2011.[3] Since July 1, 2011, the effective FUTA tax on employers for each employee is 0.6% (a decrease from 0.8%) on the first $7,000 of wages.

State Unemployment Tax Acts

States levy their own payroll taxes on employers to fund regular UC benefits and the state share of the EB program. The SUTA tax rate of an employer is, in most states, based on the amount of UC benefits paid to former employees. Generally, the more UC benefits paid to its former employees, the higher the tax rate of the employer, up to a maximum established by state law.

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[1] For details on the UC program, see CRS Report RL33362, *Unemployment Insurance: Programs and Benefits*.

[2] For details on the federal unemployment tax see CRS Report R44527, *Unemployment Compensation: The Fundamentals of the Federal Unemployment Tax (FUTA)*.

[3] P.L. 94-566 first imposed the 0.2% surtax, increasing the net FUTA tax from 0.5% to 0.7% on the first $6,000 of earnings. The surtax was to be eliminated when all advances to the states had been repaid. P.L. 97-248 extended the surtax (increasing the net FUTA tax from 0.6% to 0.8%, on the first $7,000 of earnings) until the EUCA (Emergency Unemployment Compensation Account dedicated to funding the extended benefit program) loans were repaid. P.L. 100-203 extended the 0.2% surtax for three years—until January 1991. P.L. 101-508 extended the surtax for five years—until January 1996. P.L. 102-164 extended the surtax for an additional year—until January 1997. P.L. 103-66 extended the surtax for an additional three years—until January 2000. P.L. 105-34 extended the surtax for an additional nine years—until January 2008. P.L. 110-140 and P.L. 110-343 each extended the surtax for one additional year. P.L. 111-92 extended the authorization of the FUTA surtax through June 2011.

The Unemployment Trust Fund

The UTF is designated, by law, as a trust fund in the U.S. Treasury. The designation as a trust fund is a federal accounting mechanism to directly link revenues and distributions connected to the UC programs. The UTF accounts include

- the Employment Security Administration Account (ESAA),
- the Extended Unemployment Compensation Account (EUCA),
- the Federal Unemployment Account (FUA),
- 53 state accounts,[4]
- the Federal Employees Compensation Account (FECA), and
- two accounts related to the Railroad Retirement Board.[5]

Although the UTF contains 59 separate accounts (often referred to as *book accounts*) to attribute and distribute the monies based on program purpose, the UTF is a single trust fund. The use of separate accounts solely means that revenues and distributions are directly linked to UC program purpose. The use of a single trust fund (the UTF) for all UC programs permits a balance to carry over surplus spending authority to subsequent years. The balance represents reserve spending authority available to these programs in addition to the spending authority provided by the automatic appropriation of current tax receipts. This reserve spending authority is used during recessions when UC outlays exceed UTF tax revenues, that is, when current spending exceeds current receipts. Like many of the UTF's other transactions, the balance is effectively a bookkeeping entry. **Figure 1** (at the end of this report) graphically summarizes the flow of each transaction through the UTF.

Federal unemployment taxes are credited to the ESAA. Federal taxes are dedicated to pay for UC administration grants to the states—including administration of the EB program—and the federal share of EB. Each state's unemployment taxes are credited to the state's unemployment account. State taxes are dedicated to pay for regular UC benefits and the state share of EB (under permanent law).

Typically, the EB program is funded 50% by the federal government and 50% by the states. There have been two exceptions to this cost sharing. First, P.L. 111-5, as amended, temporarily provided for 100% federal funding of EB from February 22, 2009, through December 31, 2013.[6] Second, Section 4105 of P.L. 116-127, the Families First Coronavirus Response Act (FFCRA), temporarily makes EB 100% federally financed (with the exception of *non-sharable* compensation [e.g., state and local workers]) from March 18, 2020, until December 31, 2020, only for states that receive both halves of the emergency administrative grants authorized under FFCRA.[7]

[4] The District of Columbia, Puerto Rico, and the Virgin Islands are considered to be states under federal UC law.

[5] For the purposes of this report, the Railroad funds will be ignored. The RRUI accounts are discussed in CRS Report RS22350, *Railroad Retirement Board: Retirement, Survivor, Disability, Unemployment, and Sickness Benefits*.

[6] P.L. 111-5, as amended, also included a change in the financing structure of the Emergency Unemployment Compensation program (EUC08); P.L. 111-5 had EUC08 benefits paid by the general fund of the Treasury (previous to the enactment, the benefits were paid out of the federal accounts within the UTF). For details on EUC08, see CRS Report R42444, *Emergency Unemployment Compensation (EUC08): Status of Benefits Prior to Expiration*.

[7] All states have requested their full allotment with the exception of Puerto Rico, which had met the criteria but had not requested the second allotment. Email correspondence from Employment and Training Administration analyst to CRS, June 11, 2020. For details on these grants, see the section on FFCRA in CRS Report R45478, *Unemployment Insurance: Legislative Issues in the 116th Congress*.

Additionally, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act, P.L. 116-136) created three temporary unemployment benefits: Pandemic Unemployment Assistance (PUA), Pandemic Emergency Unemployment Compensation (PEUC), and the now-expired $600 weekly Federal Pandemic Unemployment Compensation (FPUC). The CARES Act financed these temporary UI programs using general funds of the U.S. Treasury, with the funds flowing to the states via the UTF state accounts. The temporary programs were not financed through SUTA or FUTA revenue and did not impact the state account balances.

The Unemployment Trust Fund and the Federal Budget

All UC tax receipts and outlays for benefits and administration flow through the Treasury, and thus affect federal revenue, outlays, and the overall financial position (deficit or surplus) of the federal government. The UTF accounts for all UC and EB financial transactions. This accounting device (the designation as a trust fund) is used to accumulate legal spending authority that is available automatically when needed. However, the UTF does not contain financial resources. The required cash the federal government needs to pay benefits or administrative costs must be drawn from current resources through either taxation or borrowing. The revenue and the expenditures of the UC system are counted in the federal budget.

Federal unemployment taxes are deposited (for accounting purposes) into the unemployment trust fund. Following federal law, the Treasury invests all receipts—including federal and state unemployment tax receipts—in federal securities that bear interest. This investment increases the federal debt. When these securities are redeemed to pay for administration of the program, to lend funds to the states, or to pay for extended benefits, this investment decreases the federal debt.

State unemployment taxes are required to be deposited into the unemployment trust fund. Following federal law, the Treasury invests all state unemployment tax receipts in federal securities that bear interest. This investment increases the federal debt. When states pay UC benefits to unemployed individuals, the Treasury redeems those securities held within that state's unemployment trust fund account. Thus, the payment of regular state UC benefits decreases the federal debt.

If states do not have enough reserves in their UTF account, Title XII of the SSA allows the states to borrow funds from the FUA within the UTF.[8] (States may borrow from other sources although some states are prohibited from doing so under state laws.) The issuing of loans to the state would require that the FUA redeem securities. This redemption would decrease the federal debt. If the FUA is insolvent and the other federal accounts within the unemployment trust fund do not have sufficient balances to lend the funds that states need (as occurred in FY2010 through FY2015 and began again in May 2020), Title XII of the SSA allows the FUA to borrow funds from the Treasury. If the Treasury issues new securities in order to lend funds to the FUA, this will increase the federal debt. When a state pays back the state loan from the FUA, the FUA would then use those funds to repay its debt to the Treasury and the federal debt would be decreased.

Unemployment Trust Fund Revenues and Distributions

The UTF is credited[9] with revenues from three primary sources:

[8] For details on borrowing funds, see CRS Report RS22954, *The Unemployment Trust Fund (UTF): State Insolvency and Federal Loans to States*.

[9] All revenues associated with UC are deposited to the U.S. Treasury, and all UC distributions (payments) are made by the U.S. Treasury. The revenues and distributions made by the U.S. Treasury are linked to the different UC programs and purposes through the federal accounting mechanism of the UTF and its separate accounts.

- state unemployment taxes on employers,
- federal unemployment taxes on employers, and
- U.S. government agency transfers.

As noted in this report, Congress has also directed general funds to the UTF during some economic recessions.

State Unemployment Tax Revenues Are Credited to the State Unemployment Accounts Within the Unemployment Trust Fund

State unemployment account funds that are attributable to state unemployment taxes may only be used for state UC benefits and the state's portion of EB payments. State administrative costs are funded through the appropriations process from the ESAA to the state unemployment accounts and have a separate designation.[10] At the end of FY2019, states were estimated to have collected $34.6 billion while expending $26.9 billion in regular UC benefits.[11]

Federal Unemployment Taxes Are Credited to the ESAA

Each fiscal year, funds are appropriated through the federal budget process to make distributions from the ESAA for the states' costs of administering their unemployment compensation programs, and for the federal costs of administration.[12] The Secretary of Labor determines (certifies) the amount of the administrative payments, and permits the Secretary of the Treasury to make the payments from the ESAA to the states. The Secretary of Labor in certifying a state for payment takes into account (1) that the state's UC programs contain specific provisions related to the payment of monies from the state unemployment system, (2) the state agency's specific responsibilities in administering the UC program and UC benefits, and (3) the rights and responsibilities of the UC benefit recipients.

Transfers between UTF Accounts: ESAA, EUCA, FUA, and FECA

By the end of FY2019, the federal accounts had collected $5.63 billion; the ESAA had a net balance of $2.72 billion. Because the ceiling for the ESAA was $1.45 billion, $1.27 billion in excess funds were transferred to the EUCA. Each month, the ESAA distributes 20% of the *net monthly activity* to the EUCA. Net monthly activity is the sum of revenues credited to the ESAA less distributions for refunds of FUTA taxes and additional taxes attributable to a reduced credit for SUTA taxes in each month. By the end of FY2019, the ESAA had distributed a total of $5.13 billion to the states for administrative costs.

[10] For details on this process, see CRS In Focus IF10838, *Funding the State Administration of Unemployment Compensation (UC) Benefits*.

[11] Division of Fiscal and Actuarial Services, Office of Unemployment Insurance, Employment and Training Administration, U.S. Department of Labor, *Unemployment Insurance Program Outlook President's Budget 2021*, Washington, DC, February 2020, https://oui.doleta.gov/unemploy/pdf/prez_budget_21.pdf. Projected FY2020 state tax collections and expenditures did not take into account the economic shock of employment loss attributable to the COVID-19 pandemic and subsequent increases in UC outlays and decreases in revenues. Thus, this report omits those projections.

[12] For details on this process, see CRS In Focus IF10838, *Funding the State Administration of Unemployment Compensation (UC) Benefits*.

If states have an active EB program, EUCA distributions are made for the federal portion (50%) of EB payments.[13] At the end of the fiscal year after any required distribution from the ESAA, the EUCA balance is calculated. The EUCA balance is limited to the maximum of $750 million or 0.5% of covered wages.[14] If the EUCA balance exceeds the limitation, the excess is distributed to the FUA. At the end of FY2019, no funds were expended to pay for the federal share of EB benefits as no state met the economic criteria to provide an EB benefit in FY2019. The EUCA net balance was an estimated shortfall of (negative) $6.24 billion (a cash balance of $0.84 billion, $7.08 billion owed to the general fund of the Treasury). The EUCA ceiling was $33.13 billion; thus, there was no fund transfer to the FUA.

In addition to any EUCA distribution, the FUA is credited with the additional taxes paid by employers when a reduced credit against federal taxes exists because the state has an outstanding unpaid loan from FUA. FUA funds are distributed as loans to states, through the state unemployment accounts. (See the discussion below on "Loans to Insolvent Accounts" for a more detailed explanation of these loans.) The FUA balance is limited to the maximum of $550 million or 0.5% of covered wages. At the end of FY2019, the estimated net FUA balance was an estimated $10.72 billion which included $0.06 billion borrowed by the Virgin Islands and $7.08 billion owed from ESAA/EUCA, and an end of year *cash* balance of $3.57 billion). The balance was lower than the $33.13 billion ceiling and so no Reed Act distribution occurred. (See below for details of the Reed Act distributions.)

In addition, distributions are made to the state unemployment accounts from the FECA to reimburse the states for employment compensation paid to former federal employees. Each federal agency reimburses the UTF for its share of federal workers' UC benefits.

Timing of UTF Deposits

State Unemployment Taxes

Employers required to pay state unemployment taxes may remit their state unemployment taxes to states on a monthly, quarterly, annual, or other basis as determined by state laws and regulations. States, in turn, remit the collected taxes to the Treasury. These funds are credited to the appropriate state unemployment account in the UTF.

Federal Unemployment Taxes

Employers may also be required to pay FUTA taxes on a quarterly basis. If the estimated quarterly federal tax is less than $500, an employer may roll the liability over to the next quarter until the liability is $500 or more. At that point, the employer must pay the FUTA taxes

[13] With the passage of P.L. 111-5, the EUC08 program was 100% financed by the federal government through general funds within the U.S. Treasury until EUC08 authorization terminated in December 2013. Beginning in March 2020, Section 4105 of P.L. 116-127 temporarily makes EB 100% federally financed (with the exception of *non-sharable* compensation [e.g., state and local workers]) from enactment until the end of December 2020 for states that meet certain requirements.

[14] P.L. 105-33 increased the statutory ceiling on the FUA from 0.25% to 0.5% of covered wages, effective October 1, 2001. P.L. 102-318, had lowered the FUA from 0.625% to 0.25% and increased the ceiling for EUCA from 0.375% to 0.5%. P.L. 100-203, had raised the EUCA ceiling from 0.125% to .375% and increased the FUA ceiling from 0.125% to 0.625%.

to the Treasury. An annual tax return reconciles the quarterly deposits to the actual tax liability. The ESAA is credited with the federal unemployment taxes.

U.S. Government Agency Transfers

Each federal agency is responsible for Unemployment Compensation for Federal Employees (UCFE) paid on the agency's behalf. Similarly, each military service unit is responsible for Unemployment Compensation for Former (ex-) Servicemembers (UCX) paid on the service unit's behalf.[15] Each agency must budget for the unemployment benefits paid and reimburse the UTF for unemployment compensation paid on its behalf by states. The funds are credited to the FECA. Although UC benefits are taxable and are fully subject to the federal income tax, those revenues do not support the UC system and are not credited to the UTF.[16]

Other Unemployment Trust Fund Expenditures (Reed Act Distributions)

At the end of the fiscal year, there is a limitation on the balance in the ESAA—the account balance cannot exceed 40% of the prior fiscal year's appropriation by Congress. If the balance in the ESAA exceeds this limitation, the excess is distributed to EUCA. After the distribution, if the balance in the EUCA exceeds the limitation, the excess is distributed to the FUA. If after the distribution from the EUCA, the FUA balance exceeds the limitation, the excess is distributed, as a Reed Act distribution, to the states.[17] At the end of FY2019, there was no Reed Act distribution.

Loans to Insolvent Accounts

The Treasury can issue checks for a state unemployment account, provided that legal spending authority exists for such spending and if the state unemployment account has a positive balance. However, during recessions, current state unemployment tax receipts and the state account reserve balance may be insufficient to cover expenditures for the state's UC benefits.[18] Thus, state UTF accounts may require an advance (or loan) to pay for state UC benefits.

A state unemployment account may request an advance on its deposits and borrow funds from the FUA. If a state does not repay the loan within a set period, federal law requires that the principal of the loan must be repaid by reducing federal tax credits for SUTA taxes and crediting those increased revenues to the FUA.[19] The state cannot pay the interest on such loans using the state unemployment account but must instead pay the interest through state general revenues or other measures.

[15] For details on UCX, see CRS Report RS22440, *Unemployment Compensation (Insurance) and Military Service*.

[16] This differs from funds from the taxation of Social Security benefits, where the revenue is used to support the Social Security and Medicare programs.

[17] For more information on Reed Act distributions, see CRS Report RS22006, *The Unemployment Trust Fund and Reed Act Distributions*.

[18] For details on loans to insolvent accounts, see CRS Report RS22954, *The Unemployment Trust Fund (UTF): State Insolvency and Federal Loans to States*.

[19] For a list of current advances of funds to the states, see https://oui.doleta.gov/unemploy/budget.asp.

Federal law also authorizes the federal accounts to borrow funds from each other or from the general fund if balances in the federal accounts are insufficient to cover their expenditures.

- If the amount in the ESAA, FUA, or EUCA, is insufficient to meet the anticipated payments from the account and the amount in any other such account exceeds the amount necessary to meet the anticipated payments from such other account, the Labor Secretary may lend funds from one account to the other.[20]
- The ESAA may borrow from the general fund if the sums appropriated for state UC administration are greater than the ESSA balance.[21]
- The EUCA may borrow funds from the general fund for federal share of EB payments.[22]
- The FUA may borrow funds from the general fund for loans to the states.[23]

If the states' borrowing needs exceed the available FUA balance, the FUA may borrow funds from ESAA and EUCA. If the ESAA and EUCA balances are insufficient, the FUA may borrow from the general fund of the Treasury to cover the amount needed. From FY2009 through FY2015, the FUA borrowed funds from the general fund of the Treasury in order to loan funds to the state accounts. In May 2020, the FUA once again began to borrow funds from the general fund of the Treasury as states rapidly depleted their UTF accounts.

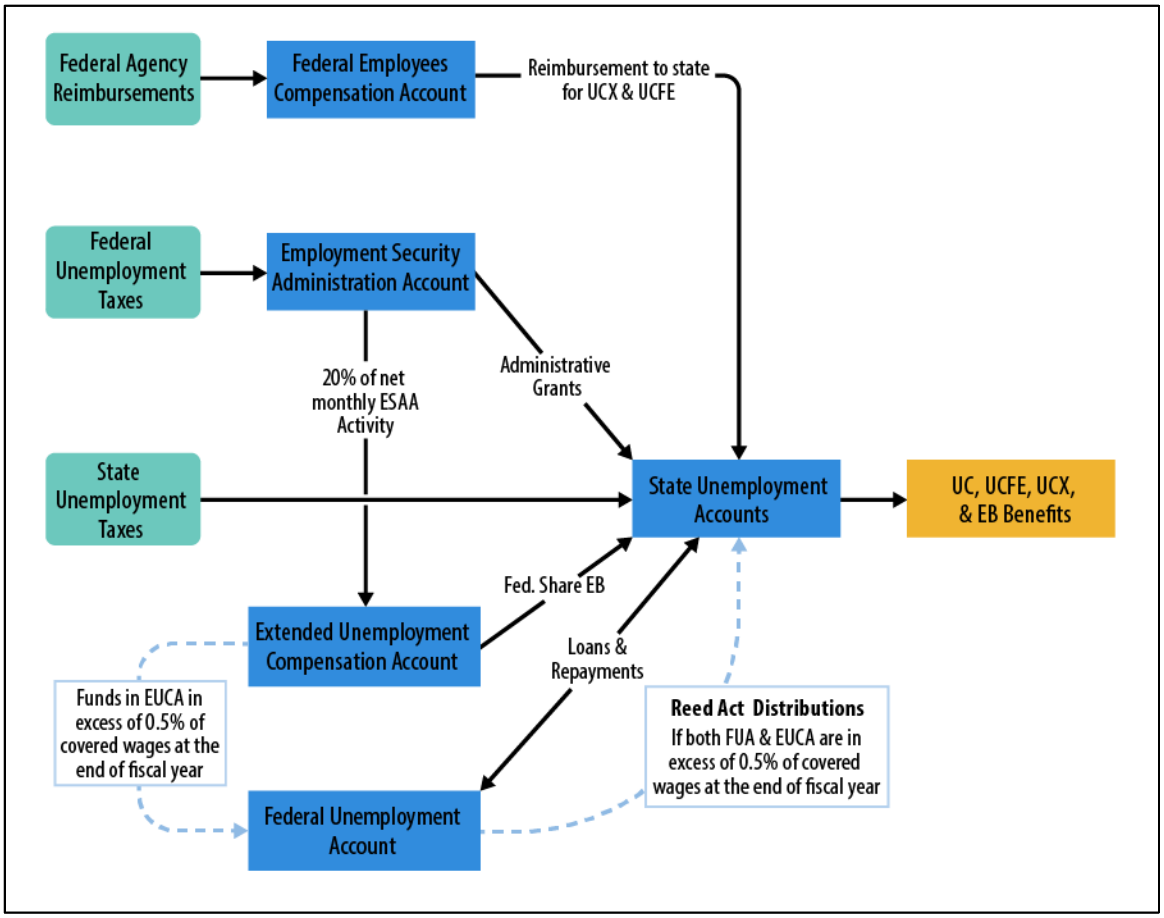
[20] 42 U.S.C. §1110(a).

[21] 42 U.S.C. §1101(e)(2) requires that if the net balance in the ESAA as of the beginning of any fiscal year equals 40% of the amount of the total appropriation by Congress to the ESAA for the preceding fiscal year, such loans would require legislative action.

[22] 42 U.S.C. §1105(d).

[23] 42 U.S.C. §1323.

Figure 1. The Unemployment Trust Fund



Source: Figure prepared by the Congressional Research Service (CRS).

Notes:
EUCA=Extended Unemployment Compensation Account
FUA=Federal Unemployment Account
UC=Unemployment Compensation
UCFE=Unemployment Compensation for Federal Employees
UCX=Unemployment Compensation for Former (ex-) Servicemembers
EB=Extended Benefits

Author Information

Julie M. Whittaker
Specialist in Income Security

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