

**ALASKA UNEMPLOYMENT INSURANCE
HANDBOOK FOR
LEGISLATIVE PLANNING**

1971 LEGISLATIVE SESSION

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ALASKA UNEMPLOYMENT INSURANCE

HANDBOOK FOR

LEGISLATIVE PLANNING

1971 LEGISLATIVE SESSION

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P R E F A C E

This publication and publication number one entitled, Alaska Unemployment Insurance Financial Handbook were designed to provide the Legislature (and others) with ready references and to present our recommendations and those of the Administration.

All costs were developed in consultation with the Office of Actuarial Services and Unemployment Insurance Research of the U. S. Department of Labor and were in accordance with standard actuarial techniques established by that office. We were also very fortunate to have the services of one of the most noted Alaskan Economists, Dr. George W. Rogers, who in 1958 worked on Alaska's most recent Actuarial Study.

This study was initiated in August 1970 as a two phase program. In the first phase our efforts were concentrated primarily on benefit financing. In the second phase we intend to look at benefit adequacy more acutely and other areas in Alaska's Unemployment Insurance program which need strengthening and improving.

J A N U A R Y 1 9 7 1

ALASKA UNEMPLOYMENT INSURANCE HANDBOOK FOR LEGISLATIVE PLANNING

1971 LEGISLATIVE SESSION

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PART I

RECOMMENDATIONS TO STRENGTHEN AND IMPROVE ALASKA'S
UNEMPLOYMENT INSURANCE SYSTEM

RECOMMENDATIONS TO STRENGTHEN AND IMPROVE
ALASKA'S UNEMPLOYMENT INSURANCE SYSTEM

The Unemployment Insurance program was created by Federal law on August 14, 1935 and enacted by Alaska law on April 2, 1937. The system is one of the foremost examples of a working Federal and State relationship. Most of the decisions about the nature of the program are left to the administering State which makes the system far more flexible and attuned to local needs and special circumstances of local economies.

The program's primary function is to alleviate the economic hardships which accompany an unemployed worker's loss of wages through no fault of his own. This is effectively accomplished when the program provides adequate wage loss replacement as a matter of earned right in a dignified and orderly manner to maintain the worker's standard of living without destroying the unemployed worker's incentive to work.

The employer pays a tax on his wages supplemented by a small employee contribution to insure against the day when the employee may be between jobs. That insurance is like a mandatory fringe benefit bought in the employee's behalf. In addition it is considered the Nation's first-line of defense to counter the deflationary effects of unemployment. By sustaining personal income it effectively combats the resulting declines in purchasing power which cause the economic downturn to gather momentum. It is recognized as an effective income or economic stabilizer. Although significant economic changes have taken place within the Nation and especially in Alaska since the program was established, the basic legislation governing the operation of the program has virtually remained unchanged since 1935.

The "Employment Security Amendments of 1970" represent the most significant Act to amend the unemployment compensation program since it was enacted in 1935 as part of the Social Security Act. Many of the above principles underlying the Unemployment Insurance program were brought out in President Nixon's message which accompanied H.R. 12625 and H.R. 14705, later to be enacted on August 10, 1970 as P.L. 91-373.

President Nixon also emphasized that the Federal government has traditionally established minimum improvements to upgrade the program and called upon the States to follow the leads of other progressive States and enact legislation to further improve their program in light of their own economic needs - to avert the need for Federal action. He expressed that the following major areas are presently deficient and deserve immediate attention to provide (1) adequate coverage to State and local government workers, (2) adequate benefits, and (3) economic responsiveness.

It was the expressed policy of our legislature through the enactment of Alaska's Employment Security Act to carry out essentially all of the above objectives. With those principles and guidelines in mind and after reviewing carefully the President's recommendations, we encourage the Alaska Legislature to enact the following legislation and recommendations to strengthen and improve Alaska's Unemployment Insurance program.

- 1) We should extend unemployment insurance protection to an estimated 18,000 workers in State and local government.
- 2) We should rectify the present inadequate benefit structure which compensates on the average only 21 percent of the unemployed workers' wage loss.
- 3)
 - a. We should increase the responsiveness of the financing and benefit structure to major changes in Alaska economic conditions - to assure adequate benefits and sound-equitable financing under every economic situation.
 - b. We should strengthen the financing structure to achieve a balance of income and expense over a period of time, whereby the employer and employees' costs are spread over the business cycle by collecting in "good times" to pay for "bad times".
 - c. We should establish and enact a measure of fund adequacy to assure payment of adequate benefits under all economic conditions, without building up an "over-adequate" or an "under-adequate" reserve at the expense of the employer and employee.
- 4) We should improve the financing of the system which presently discriminates against the low-wage worker, in some cases the small and in other cases the large employer.

The coverage extensions currently proposed provide a significant advance toward bringing into the program workers in need of wage loss protection.

ALASKA

PRESENT AND PROPOSED UNEMPLOYMENT INSURANCE COVERAGE OF WAGE AND SALARY EMPLOYMENT

Calendar Year 1969

INDUSTRY DISTRIBUTION

INDUSTRY DISTRIBUTION	NUMBER	PERCENT
<u>Commodity Producing</u>	17,346	17.6%
Mining	3,494	3.5
Contract Const.	6,555	6.8
All Manufacturing	7,023	7.1
Ag., Forestry & Fish.	174	.2
<u>Distributive</u>	34,290	34.9%
Trans., Comm. & Util.	8,644	8.8
Wholesale & Retail Trade	13,947	14.2
Fin., Ins. & Real Est.	2,651	2.7
Services	9,048	9.2
<u>Government</u>	17,359	17.7%
Federal	16,451	16.7
State	661	.7
Local	247	.3
<u>Noncovered (estimated)</u>	29,300	29.8%
Self Employed & Un-	7,900	8.0
paid Family Workers	150	.2
Canadian Railroad	800	.8
Agriculture	3,050	3.1
Domestic Service	1,450	1.5
Nonprofit Inst.	7,300	7.4
Local Government	8,650	8.8
State Government		

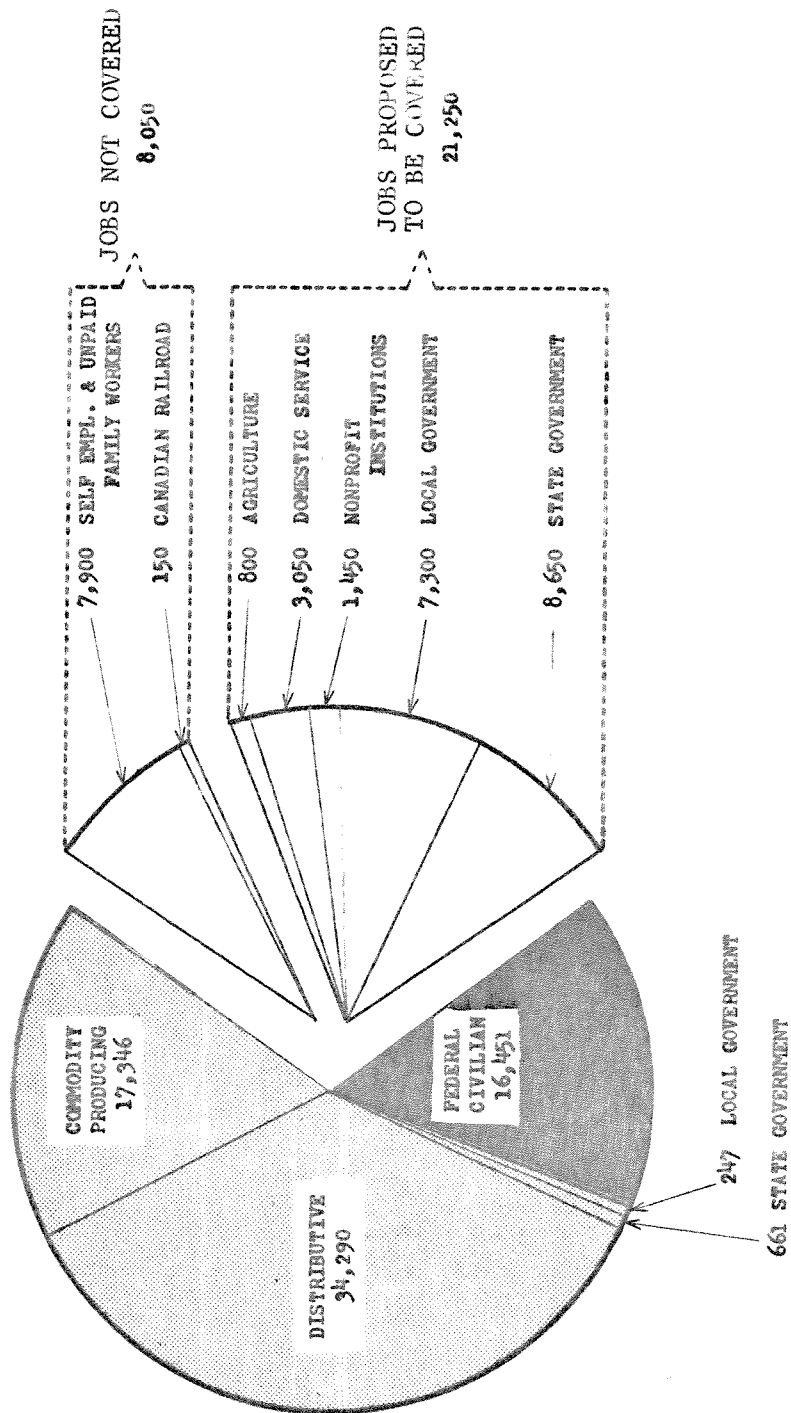


Chart 1.

PART II

ALASKA'S ECONOMY 1939-1980 - TRENDS AND COMPOSITION

ALASKA'S ECONOMY 1939-1980 - TRENDS AND COMPOSITION

Over the life of the Alaska unemployment insurance program, the Alaska economy has grown in size and diversity, undergone several major changes in industrial composition and experienced periods of boom expansion followed by recession. The nature of these changes in industrial composition and growth rate and trends in the economy have had important implications for the operation of the program. Refer to Chart 2.

The Forties - Exchanging Specializations, from Salmon and Gold to Defense

At the time of the enactment of the first program in 1937, Alaska's economic value to the nation was as a source for fisheries products (primarily canned salmon), and minerals (primarily gold and to a lesser extent, copper). Other resources were harvested and values produced, but the economy was a very narrowly specialized one with a past history of a turn-of-the-century gold rush followed by a long period of stagnation. In 1939 average monthly employment was about 30,000 persons, approximately a third being fishermen and other self employed persons. The two thirds of the employed workforce receiving wage and salary compensation was concentrated in trade and other distributive industries (19% of total employment), mining (15.5%) and manufacturing (15.9%). Government, including defense, accounted for 12.4% of total employment.

Following the invasion of the Aleutian Islands in 1942 and continuing to the present, Alaska's main national importance has been its strategic defense location. From a pre-war total of 500 officers and men, military personnel stationed in Alaska rose to 152,000 by July 1943, stabilizing at about 50,000 in the early 1950's. Average monthly employment covered by unemployment insurance rose from 10,916 in calendar year 1940 to 20,540 in 1942 and total annual covered wages from \$20.2 million to \$51.4 million. Most of this increase was in contract construction and other defense related activities. Gold mining was completely suspended under war manpower programs and fisheries declined as the resource yield fell.

The Fifties - Construction Cycles, Creating the Defense System

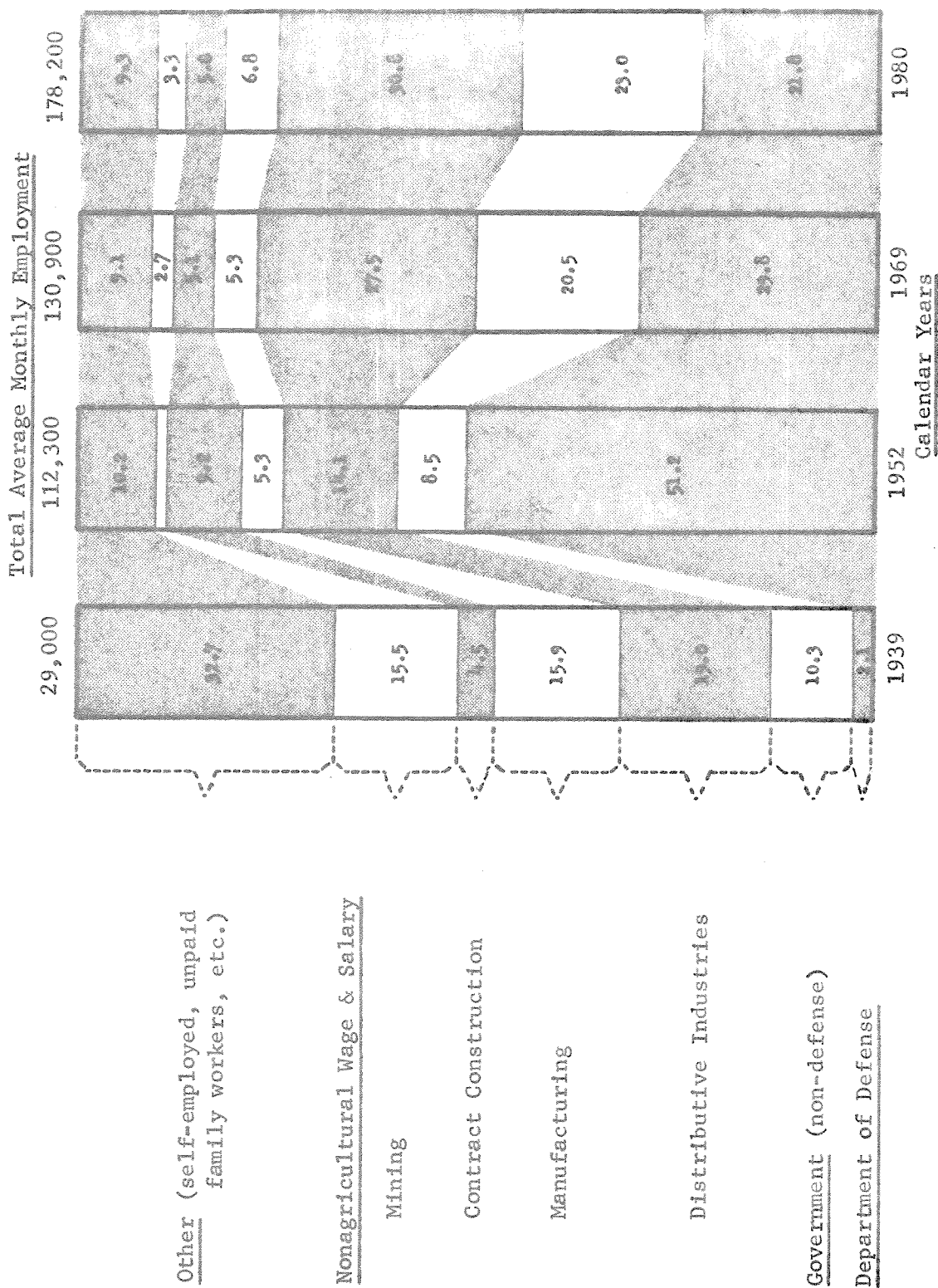
During the 1940's and the 1950's Alaska had a defense and federal government oriented economy. Calendar year 1952 is typical. Of the total employed workforce of 112,300 persons per month, Department of Defense (military and civilian personnel) accounted for 51.2%, other government 8.5%, distributive industries (strongly related to or derived from defense activities) 14.1%, and contract construction 9.2%. Mining had fallen to 1.5%, manufacturing to 5.3% and non-wage and salary employment to 10.2%.

Total employment climbed sharply during the 1940's, but assumed a relative plateau during the 1950's, reaching approximately 62,000 persons in calendar years 1951, 1952, 1956, 1957, and 1959, and dropping significantly below these levels in the other years of the decade. The most serious recession

Chart 2 .

COMPOSITION OF TOTAL EMPLOYED WORKFORCE BY MAJOR INDUSTRY
1939 - 1980

The Alaska economy has grown in size and diversity, undergone several major changes in industrial composition and experienced periods of boom expansion followed by recession.



occured between 1957 and 1959 following completion of major defense construction programs. Within the major industrial classifications, military personnel declined from 50,000 in 1952 to 34,000 by 1959, but a steady increase in employment was experienced in civilian government at all levels. Distributive industries and manufacturing remained relatively constant, and mining continued to decline. Contract construction average monthly employment fell from a high of 11,500 persons in calendar year 1951 to 5,100 in 1958, and 4,800 in 1959. This imposed a boom and bust pattern upon both the total economy and the unemployment insurance program.

The Sixties - Diversification and Growth, Petroleum and Forest Products

During the 1960's defense continued as the main stay of the Alaska economy, but natural resource products represented a growing element with establishment of a wood pulp industry in southeast and petroleum industries in southcentral Alaska. The estimated gross value of all natural resources products rose from \$130.6 million in calendar year 1950 to half a billion dollars by the end of the sixties. The outlook is that these values will probably exceed two billion dollars by 1980. Spending by the Department of Defense, on the other hand, declined and assumed a fairly constant level at about \$350.0 million annually.

In spite of this marked change in output, the total level of employment in all commodity producing industries (mining, construction, and manufacturing) remained relatively constant, with oil and gas increases offsetting other mining declines and forest products offsetting food processing declines. The most dynamic source of growth and change in composition of the total economy came from distributive industries and non-defense government employment. The increase in cyclical stability represented by these industries was in part offset by the instability of the new employment in oil and natural gas. During the initial exploration and development phases this industry employed relatively large numbers of persons, but during the periods of field consolidation and production the level of employment falls significantly. In the development of the initial North Slope field, for example, mining employment rose to more than 4,000 between July through September 1969, but for the same period in 1970 the level of mining employment was only about 2,500.

The Seventies - Continuing Growth and Instability

The general outlook for the 1970's is continued overall growth (from a monthly average total workforce employment of 130,900 in 1969 to 178,200 by 1980), continued decline in the relative importance of Department of Defense employment (from 29.8% to 21.8% of total employment) and cyclical fluctuations in oil and gas employment (a characteristic of the development to production transition) and in contract construction (primarily due to a brief period of intense activity associated with pipeline or other petroleum related construction).

PART III

EXTENSION OF UNEMPLOYMENT INSURANCE COVERAGE TO STATE
AND LOCAL GOVERNMENT EMPLOYEES

EXTENSION OF UNEMPLOYMENT INSURANCE COVERAGE TO STATE AND LOCAL GOVERNMENT EMPLOYEES

In 1969, 54 percent of the estimated number of workers not covered by unemployment insurance in Alaska were employees of state or local government. It is time now for Alaska to join the ranks of other progressive states which have taken action to provide mandatory coverage for all state and local government workers.

What Government Employees are Presently Covered and What Does it Cost?

Coverage of federal employees, beginning January 1, 1955, gave impetus to some states to initiate similar action; however, constitutional limitations prevented imposing federal taxes on wages earned in state and local government employment. By the mid-sixties, ten states had enacted legislation extending mandatory coverage to state employees and financing benefits on a reimbursable basis. Two of these also extended mandatory coverage to local government employees. At this time, 34 states provide some sort of coverage, either mandatory or elective, for state and local government employees.

Although private industry and state and local government are engaged in different activities, many of the occupational requirements are similar. Governments employ accountants, clerks, engineers, equipment operators, administrative personnel, and people with many other different skills, as do the private industries. All of the employees we are recommending for coverage would already be covered if they had been employed in private or federal government employment. We should also bear in mind the loss of unemployment insurance protection to employees of the Bureau of Indian Affairs educational and other facilities when they are taken over by the State of Alaska.

Actual experience of ten states with mandatory coverage reveals cost rates ranging from .12 to .68 percent of total wages. Alaska's experience with the coverage of about 700 employees in the Marine Transportation and Employment Security has shown a cost of .3 to .8 percent of total payroll. These rates, combined with the experience of Unemployment Compensation for Federal Employees, demonstrate that a real unemployment problem does exist among government workers.

Do Government Employees Experience Unemployment?

In the early years of unemployment insurance, government workers were excluded from coverage because it was believed that (1) civil service systems offered special protection from involuntary unemployment, (2) raising taxes and budgets to finance such coverage created an unfavorable political climate, and (3) little public concern was generated when unemployment occurred in government. However, personnel cuts have to be made when appropriations are reduced. A good example of this is the recent cutback in government employment in the State of Washington as a result of recessionary conditions. Also, workloads and employment fluctuate in some government operations - and even while total government employment may be increasing, jobs are lost through changes in operating methods

or shifts in activities. Although, generally, government employment is steady, federal government coverage has shown that workers, especially those in manual occupations, experience a considerable amount of unemployment. Government workers do suffer involuntary unemployment and subsequent wage loss which should be compensated.

Who Should Receive Coverage?

It is the objective of Unemployment Insurance to cover only positions that are considered subject to involuntary unemployment. This would exclude any elected or appointed officials not in the classified or partially-exempt ranks of the State personnel system. Persons elected or appointed to office (and their electors and appointers) do have some control over their employment, therefore, their unemployment experience could not be considered involuntary. It was also not the intent of Unemployment Insurance to cover officials whose unemployment resulted from a change in administration or a decision not to run. Those employed on a fee basis are not recommended for coverage, nor are patients and inmates employed in state institutions, or members of boards, commissions or authorities since they do not have a firm attachment to the labor market.

Since we are required to extend coverage this year to employees at the University of Alaska, Alaska Psychiatric Institute, Harborview Memorial Hospital in Valdez, and other not presently covered nonprofit organizations to conform to P. L. 91-373, it would be wise to include at the same time employees of other similar institutions. 1/ We should extend coverage to employees in other state-operated schools, who have occupations similar to those of employees at the University of Alaska. They would certainly be subject to involuntary unemployment and would have as firm an attachment to the labor force and should be covered at the same time.

What is Extended Coverage Worth to Alaska?

If unemployment insurance coverage were extended to state and local government employees, 18,000 more Alaskans would have the added protection of compensation for wage loss during spells of involuntary unemployment. To avoid double taxation, we recommend financing for state government employees be on a reimbursable basis. Therefore, the only state cost involved would be the actual cost of benefits. We recommend that local government share in the costs of the program as any other employer. This money would not be considered an unwise investment whether its original source is the people and employers of Alaska or interest from investments. The value received by government employees and by the Alaskan economy unquestionably outweighs the cost of this extended coverage.

1/ We are also recommending repeal of our present statute which excludes coverage of service performed by nurses, technicians, and other professional employees of hospitals (A.S. 23.20.525 (4)). This would give these individuals the same unemployment protection as employees at Alaska Psychiatric Institute and Harborview Memorial Hospital.

Table 1

SIGNIFICANT FINANCIAL CHARACTERISTICS CONCERNING U.I. COVERAGE
OF ALASKA STATE AND LOCAL GOVERNMENT EMPLOYEES

Year	Avg. Empl.	Total Payroll	Taxable Payroll	Percent Taxable	C O N T R I B U T I O N S		BENEFITS
					Total	Employer	Employee
STATE ^{1/}							
1966	445	\$3,908,626	\$3,244,532	83.0	\$ 62,709	\$ 52,236	\$10,473
1967	481	4,312,586	3,406,530	79.0	94,130	78,139	15,991
1968	552	6,011,926	4,529,918	75.3	130,683	108,441	22,242
1969	660	7,256,896	5,061,357	69.7	145,139	120,440	24,699
LOCAL ^{2/}							
1966	153	\$ 899,929	\$ 791,916	88.0	\$27,426	\$22,564	\$ 4,862
1967	238	1,300,087	1,154,760	88.8	43,650	35,903	7,747
1968	209	1,382,205	1,225,026	88.6	48,644	39,961	8,683
1969	247	1,487,616	1,262,890	84.9	49,480	40,631	8,849

^{1/} Includes coverage elected by the Marine Transportation and Employment Security Divisions out of an estimated 9,300 State employees in 1969. About 2,000 will be extended coverage at the University of Alaska, Alaska Psychiatric Institute and Harborview Memorial Hospital in Valdez.

^{2/} Out of about 7,600 employees in local government this sector includes coverage elected by smaller communities only.

PART IV

FINANCING ADEQUATE BENEFITS THROUGH EQUITABLE TAXATION

BOOM TO BUST AND REMEDIAL LEGISLATION

Alaskans familiar with the recessions of the fifties may recall with some bitterness the U.I. fund's inadequacy in meeting benefit payments after the "boom" economy of the early years of that decade. Because of actuarial deficiencies in the insurance program, Alaska's U.I. fund went broke in 1955 and \$13,565,000 (about one-third of the present balance in our fund) in loans were procured from 1955 to 1960 to keep the program alive. Besides the additional cost to Alaskan employers to pay back these loans, interest to the extent of almost one million dollars was lost.

As a result, amendments focused primarily upon the financing rather than benefit aspects. Measures to improve the financial conditions of the fund were enacted in 1955 and 1960. In 1955 an employee contribution of .5 percent was implemented and the tax base was raised from \$3600 to \$4200. In 1960 the employer contribution was increased from 2.7 to 2.9 percent, the employee contribution to .6 percent, and the tax base to \$7200. As a result, taxes were increased a total of .8 percent and the tax base was doubled during the recessionary periods of 1955 and 1957-58, periods when there was not only "less wages to tax" but increased contributions were required when the employer and employee "could least afford" them.

These measures followed shortly after the "boom economies" of 1950-1952 and 1955-1957 when substantial employment was required to build up Alaska's defense immediately following World War II and during the Korean war. These supposedly "good" economic conditions soon evolved into severe unemployment as jobs to buffer the superficially stable economic growth were nonexistent.

ADEQUATE BENEFITS

Since the enactment of measures for the fund's financial improvements in 1955 and 1960, Alaska's benefit structure continued to be neglected. Slight improvements were made in 1966 and 1969 maintaining the current inadequate ratio of weekly wages but not improving it. At best, in 1972, with our current tax yield and P.L. 91-373's increased cost, we can only compensate in benefits 21 percent of the average worker's wage. As is noted in Chart 2, Alaska's benefit structure has not kept pace with wage trends, much less a more rapidly rising cost of living.

When our fund went broke in 1955, this ratio was .29 as compared with .43 in 1939. For the entire period from 1939 through 1955 the claimants' weekly benefit compensated about .30 of the average weekly wage. Since we experienced very severe recessions in 1955 and 1958, benefits could not be increased and the ratio fell to .24 in 1960. As our fund became more solvent, benefits were increased slightly in 1966 and 1969. In 1966 the maximum annual earnings requirement for eligibility was raised, however, from \$4000 to \$5000 and to \$5500 in 1969. This maintained a ratio of about .23 until 1969 when it dropped to .22. By conforming to the Federal U.I. law our ratio is expected to be .21 in 1972 and will continually decrease unless benefits are increased.

Explanation of the Proposed Benefit Legislation Incorporating a Flexible Maximum Weekly Benefit Amount.

The proposed legislation will make Alaska's benefit schedule economically sensitive by maintaining the maximum basic weekly benefit amount each year as a percent of Alaska's average weekly wage. By so doing the Alaskan claimants' average weekly benefit amount will increase as wages increase. The purpose of a flexible maximum, therefore, is to maintain each year the same ratio of the average weekly benefit to the average weekly wages.

How does Alaska's Benefit Schedule Compare to Other States?

The ratio of Alaska's average weekly benefit to average weekly wages is lower than any other state. In 1969 Alaska's ratio was .22, compared to .34 for the U.S. average. The next state in rank was .24. Although Alaska has a considerably higher average Weekly Wage (\$207 in 1969 versus \$159 for the nearest state), there are 18 states who have maximums, excluding dependency allowances, at least as high as Alaska's maximum of \$60.

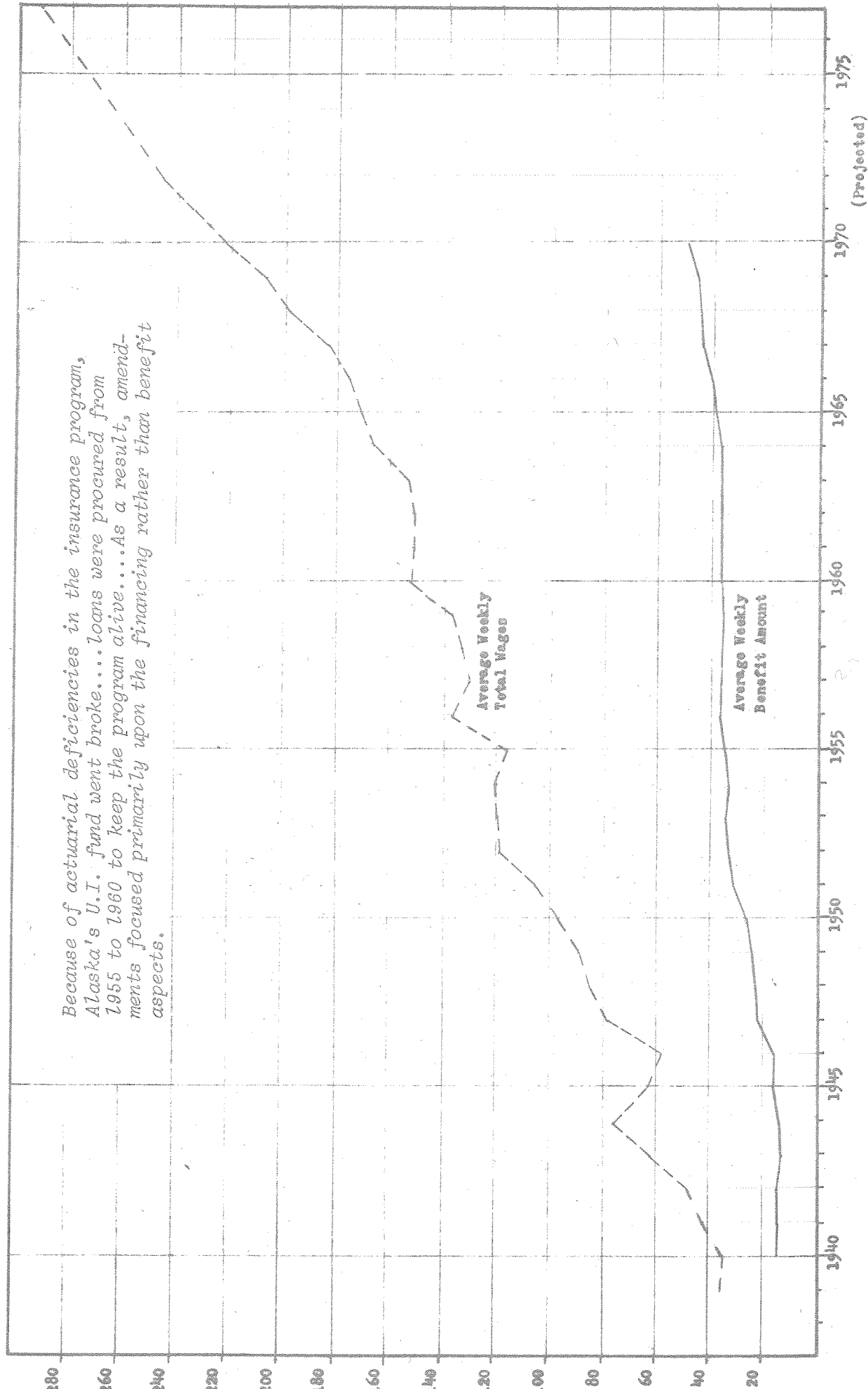
What is the Amount of Wage Loss that Should Be Compensated through U.I.?

President Nixon, in his accompanying message to Congress, noted the generally accepted principle that a State benefit schedule is considered adequate if the majority of claimants receive at least 50 percent of their average weekly wage. This is considered the minimum amount necessary to meet the nondeferrable expenses (food, shelter, etc.) of the majority of workers. To achieve this he requested states to set their maximum each year at 66 2/3 percent of the average weekly wage. Twenty-one states presently have flexible maximums of at least 50 percent, three have flexible maximums of 60 percent and one, Hawaii, sets its maximum at 66 2/3 percent.

Ideally, benefits for all claimants should increase as prices and expenses go up. If the claimant's weekly benefit is not increased as his nondeferrable expenses go up, he will not have an adequate benefit to sustain him and the economy while he is looking for work.

ALASKA AVERAGE WEEKLY TOTAL WAGES AND AVERAGE WEEKLY BENEFITS 1939-1977

DOLLARS



Could Alaska Afford a Maximum Triggered at 66 2/3 or 50 Percent?

For the majority of claimants to receive 1/2 their average weekly wage it would place at this time what we feel would be an unreasonable tax burden on the employer and employee. Alaska could afford to trigger its maximum at 50 percent and maintain an adequate reserve with a tax yield of 2.7 percent of total wages, resulting in a ratio of the average weekly benefit amount to average weekly wages of 30 percent.

How does a Flexible Benefit Schedule Work and How Would it be Financed?

This legislation is designed to maintain a reasonable relationship between the average weekly benefit and the average weekly wages. This is achieved by extending the maximum annual earnings requirement for eligibility at the same time the maximum weekly benefit amount is increased. For example:

Presently the maximum annual earning requirement is \$5500 at a basic weekly benefit amount of \$60. Assume every weekly benefit amount is increased \$5. If the average weekly wage in fiscal year 1971 is \$220 and our maximum is set at 50%, we would extend the annual earnings intervals effective January 1, 1972, as follows:

Total Base Period Wages Columns (A)	Basic Weekly Benefit Amount (B)	
\$5500 and over	\$ 60	Present Law
\$5500 - 5600	\$ 65	
5600 - 5700	66	
5700 - 5800	67	
5800 - 5900	68	
5900 - 6000	69	
6000 - 6100	70	
-	-	
7000 - 7100	80	Proposed
-	-	
-	-	
8000 - 8100	90	
-	-	
-	-	
9000 - 9100	100	
-	-	
-	-	
9500 - 9600	105	
9600 - 9700	106	
9700 - 9800	107	
9800 - 9900	108	
9900 - 1000	109	
\$10,000 and over	110	Law

The maximum would equal 50% of \$220 or \$110. Each year the calculations would be made and the schedule adjusted accordingly.

The cost of the example could easily be absorbed without jeopardizing the fund's adequacy by a tax system yielding 2.7 percent of total wages for a reserve multiple of 1.5. Refer to Page 22 in The Reserve Multiple Tax Concept Section.

With this tax yield the cost of the above example would not cause our reserve multiple to fall below 1.20 unless the Average IUR for the 1972-1977 Actuarial Planning Period is greater than 9% (refer to the commentary in the Benefit Cost section on the reserve multiple and the Actuarial Planning Period). Therefore, our recommended tax structure yielding an average contribution rate of 3.0 (2.5 employer and .5 employee) in 1972 for a reserve multiple between 1.2 and 1.4 could pay for the legislation enacting the above example.

Incorporation into our present schedule of a 50% maximum and a \$5 increase in every weekly benefit amount would maintain the ratio of the average weekly benefit to average weekly wages at .30 in calendar year 1972.

A Step Toward Adequacy and the Future

The present 21 percent of wage loss that is compensated through Alaska's unemployment insurance program falls far short of meeting 50 percent of the unemployed workers' nondeferrable expenses.

We are recommending what we feel are the most reasonable and minimum improvements to our schedule. The maximum would be set each year at fifty percent of the previous fiscal year's average weekly wage. To eliminate the compression at the maximum annual earnings requirement where better than fifty percent of the claimants are found, we are recommending raising the maximum to \$10,000 bringing increased earned benefits to about 50 percent more claimants. We are also recommending a general improvement across the board by raising weekly benefits to all claimants by \$5.00.

In conjunction with our recommended tax structure these barest of measures would raise and maintain each year the amount of wages compensated under the old schedule from 21 percent to 30 percent, placing Alaska's schedule close to the national average of 34 percent, without jeopardizing the fund. Although hardly a respectable advance, these recommendations would at least be an attempt to achieve a more adequate benefit than presently available for an unemployed Alaskan, at a reasonable cost to the Alaskan employer and employee.

The present high social emphasis being placed on benefits under the Unemployment Insurance System and recognition of their inherent anti-recessional effects upon the total economy will undoubtedly result in the enactment of Federal benefit standards in the very near future. These improvements will not only offset a severe cut in an Alaskan worker's standard of living when he is between jobs, but would also be a step in the right direction now in significantly lessening the future employer and employee tax burden to meet the inevitable costs of anticipated Federal benefit standards, which promise to be considerably higher than our recommendations.

RESERVE MULTIPLE TAX CONCEPT

The financial soundness of an Unemployment Insurance program is measured by the adequacy of its reserve to meet all future unforeseen contingencies or liabilities. One must recognize that recessions will occur and a tax structure should be designed to lessen the tax burden placed on the employer and employee when economic conditions are severe. It should also be designed so that the tax burden is shared in an equitable manner. The ultimate objective is to design a tax structure which is responsive to economic conditions and balances income and expense over a period of time on an equitable basis. This type of tax structure would always assure solvency; it would be economically sensitive; and it would spread costs over a period of years thereby eliminating an excessive increase in tax having to be absorbed in one year. We have designed such a tax system.

Following the lead of other states who have achieved an equitable balance of income and expense over a period of time, we have established an Actuarial Planning Period for Alaska. The objective was to pick a Planning Period which would be long enough to capture one full economic business cycle. In consultation with the U. S. Department of Labor's actuaries, we chose a Planning Period beginning in 1972 and ending in 1977. Economic assumptions were prepared and the necessary cost factors to determine a benefit cost rate for the period were developed. In a nutshell we have designed a tax structure which will meet the costs of our recommended benefit structure during the 1972-1977 Planning Period under any probably range of economic conditions. The basic principles are explained in the following sections.

How does this System Measure Fund Adequacy?

The Federal Government has suggested as a guideline in considering adequacy of a state reserve fund in relation to potential recession costs, that a state Unemployment Insurance fund should have a reserve as a percent of the latest twelve-months total wages of 1.5-3.0 times the ratio of benefits to total wages in the highest cost twelve-month period experienced since 1957. It is further emphasized that from the standpoint of an individual state, the use of the reserve multiple in conjunction with the state's economic and industrial characteristics should provide a good gauge of reserve fund adequacy. In general, however, a reserve multiple of 1.5 indicates a minimum adequate reserve level necessary to meet the full cost of a recession.

Currently about 33 states have reserve multiples above 1.5 and the national average is 1.65. We are recommending that Alaska adhere to this criteria and base its measure of adequacy on the twelve-month high cost period ending August, 1958 when the rate experienced was 4.33 percent. The economic characteristics of this period should most closely reflect the potential recessionary conditions most likely to be experienced in the oil-related economy of the future.

With this fund adequacy measure we feel that our fund would have adequate enough protection against the large recessions in addition to recessions following one after the other as occurred in 1955, 1957-58, and 1961.

How are the Principles of Sound Financing Achieved?

This system can be considered a sliding-scale taxation concept. To achieve our recommended level of adequacy we assign the benefit cost rate plus the amount necessary to maintain adequacy, as wages increase, to the interval which contains our

ALASKA COVERED EMPLOYMENT AND WAGES 1939-1977

EMPLOYMENT
(THOUSANDS)

WAGES
(\$ MILLION)

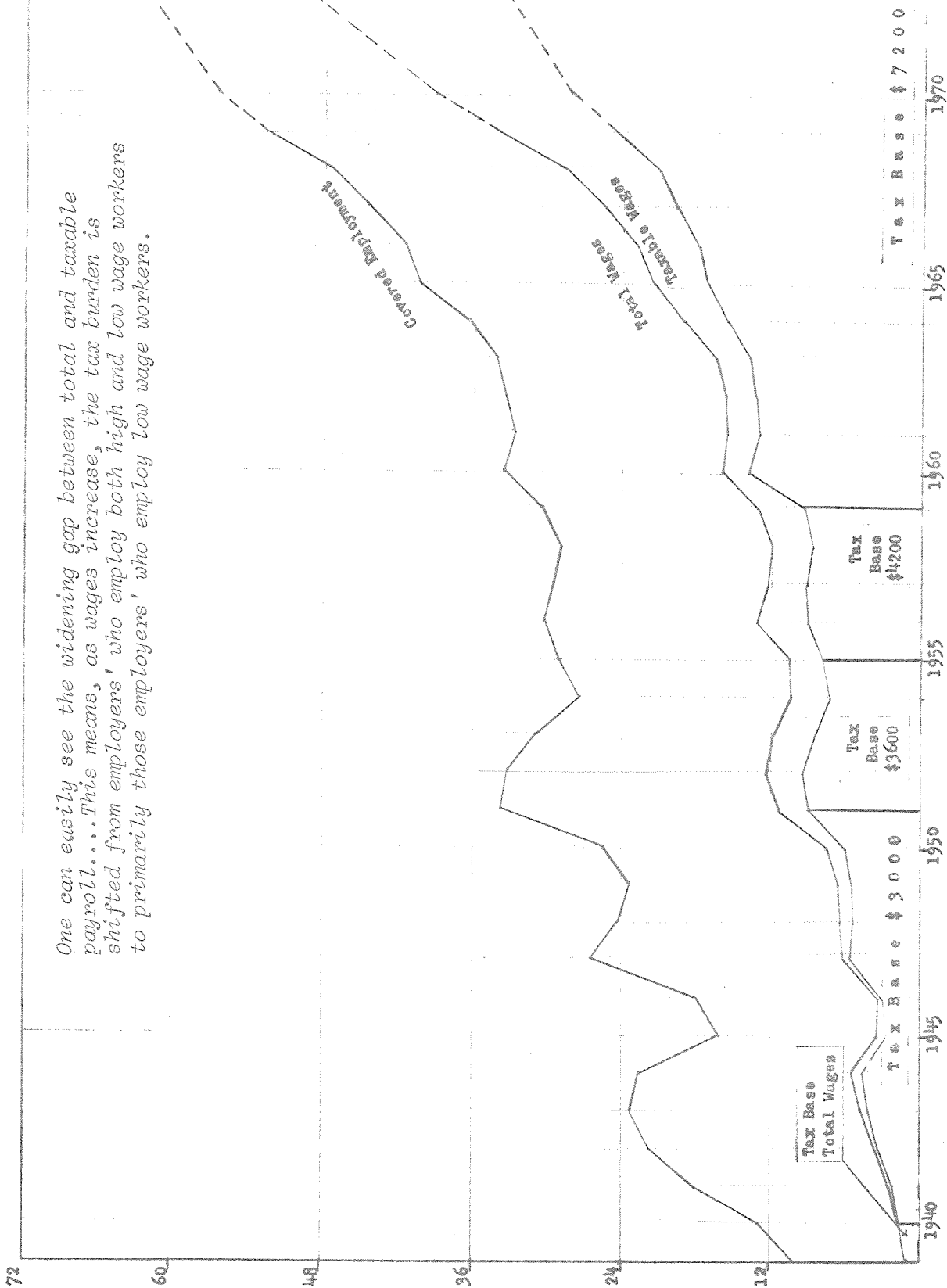
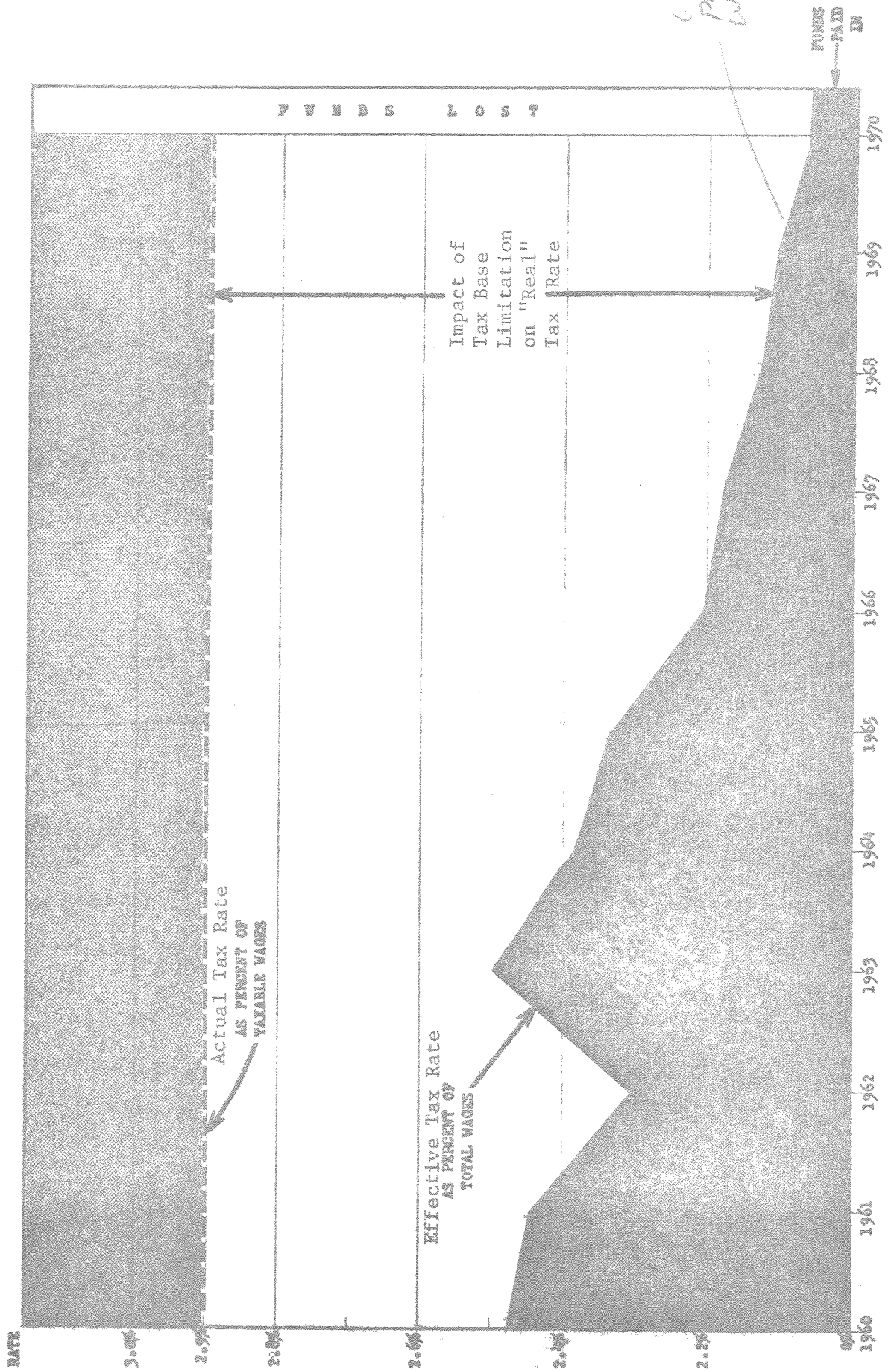


Chart 4.

LIMITED TAX BASE CAUSES REDUCTION IN THE EFFECTIVE "REAL" TAX PAID BY EMPLOYERS



recommended reserve multiple of 1.5. A reserve multiple of less than 1.5 indicates a fund which is less than adequate to meet recessionary costs and a multiple greater than 1.5 designates a safe level at which the fund can be trimmed through tax reductions.

It is economically responsive in that the measure of adequacy, the reserve multiple, is calculated each year and a higher tax rate assigned for the following rate year if poor economic conditions were experienced and a lower tax rate if good economic conditions were experienced. In so doing the tax necessary to meet the high costs experienced during the period are spread over the entire period and are shared by all employers. On the other hand, when more than enough is available to meet benefit costs, taxes are reduced to provide the employer and employee with an immediate tax advantage. For example, if the plan were made effective immediately and our recommended tax structure contained ten tax schedules, yielding specified average tax rates, the following system would be designed:

ROW	AVERAGE TAX YIELD	IF THE RESERVE MULTIPLE OF THE FUND IS:										
		Equal to or More Than	0	.5	.8	1.0	1.2	1.4	1.6	1.8	2.0	3.0
		Less Than	.5	.8	1.0	1.2	1.4	1.6	1.8	2.0	3.0	
A.	Employer		3.8	3.4	3.1	2.8	2.5	2.3	2.1	2.0	1.8	1.6
B.	Employee		.7	.6	.5	.5	.5	.4	.4	.3	.3	.2

The tax rate or yield necessary to meet the costs over the Planning Period of our recommended benefit structure is assigned to the interval containing the 1.5 reserve multiple. Based on an insured unemployment rate of 8 percent, we have predicted if this law were to go into effect January 1, 1972, our reserve multiple would be about 1.33 on September 30, 1971 calculated as follows:

Estimated Balance of the Fund on September 30, 1971 = \$39.5 Million

Estimated Total Wages For the Twelve Months Ending June 30, 1971 = \$687 Million

E Q U A L S

5.75%, Reserve Percentage

D I V I D E D B Y

4.33%, The Twelve-Month High Cost Rate Experienced For The Period Ending August 1958

E Q U A L S

1.33, The Estimated Reserve Multiple On September 30, 1971

For a reserve multiple of 1.33 the average employer contribution rate would be 2.5 percent and the employee .5 percent for rate year 1972. As a comparison, our reserve multiple for December 31, 1970 was about 1.21.

If good economic conditions are experienced in 1971, at a 7 percent insured unemployment rate the reserve multiple on September 30 would be about 1.42 - triggering an average employer contribution rate of 2.3 percent and an employee rate of .4 percent for rate year 1972.

According to our estimates, with an insured unemployment rate of 7 percent in 1972, by 1973 our fund would achieve the level of adequacy we consider safe for rate reduction, a reserve multiple of 1.5. We anticipate an average employer contribution rate of 2.1 and an average employee rate of .4 percent will be effective for rate year 1973 if expected good economic conditions are experienced. This would result in an average rate reduction of .2 percent for employers after one year's experience with the new tax structure. Also, inherent within the design of the tax structure is its capacity to recouperate quickly. Since a fund's reserve multiple will decline faster as the recession gains momentum (a snow balling effect) than it increases when economic growth is experienced, we have assigned greater increases between rates for the smaller reserve multiples.

Another Step Forward and The Future

With the recommended tax structure in effect during 1972 we expect the fund to achieve an adequate level by 1973, the reserve multiple increasing from 1.21 at the end of 1970 to 1.50 at the end of 1972. This would be accomplished even with the increased cost of conforming to the federal legislation during 1972. Having reached this adequate level further economic growth would result in rate reductions. As noted in the Alaska Economy section, this anticipated growth will also bring, as it did in the past, substantial unemployment following periods of rapid expansion.

Recalling the significant increase in unemployment in 1970 ^{1/} as a result of the sharp rise in employment related to the initial oil exploration phase, one can easily foresee the potential oil related unemployment which will definitely accompany the development - production transition in the latter years of our 1972 - 1977 Actuarial Planning Period. By maintaining an adequate fund with a reserve multiple of 1.5 through the beginning years of this Period, we should be able to weather the potential recessionary conditions of the Seventies. By so doing we will have spread the costs over the period collecting in the "good" years to pay for the "bad" years, preventing the need for remedial legislation which immediately places the tax burden on the employer at a time when he can least afford to pay.

^{1/} The insured unemployment rate in 1969 was 6.8 percent. The same rate is expected to be 8.4 percent for 1970.

EQUITABLE TAXATION

We must look at the Unemployment Insurance system as a benefit to everybody, not just the unemployed worker, and recognize the significant role that unemployment insurance plays as an income stabilizer in the economies of Alaska and the nation by maintaining purchasing power in bad times as well as good. Full employment is an impossibility in our current economy. Unemployment will continue to be experienced just as it has since 1935 when the program was initiated to relieve the economic hardships which accompany it. The cost to combat this social burden should be shared equally by all the participants in the economy. Whether a low wage worker or a large employer, the equivalent "proportion" of wages taxed should be the same as should the tax rate itself.

There should be no difference between the low wage fishery employer or employee taxes than those of a bank, drug store or service station, who just happen to have selected an occupation which provides stable year-round employment.

What Has Been the History of Alaska's Tax System?

Under the "Federal Additional Credit Provisions", through experience rating a State is allowed to reduce Unemployment Insurance taxes below the standard rate and still maintain the maximum credit against the Federal Unemployment Insurance tax for an employer with at least one year of payroll experience. Therefore, on July 1, 1947, Alaska enacted an annual payroll decline experience rating formula. This formula was in effect through June 30, 1952. No experience rating system was in effect from July 1, 1952 through September 30, 1960. On October 1, 1960, a quarterly defined payroll decline formula became effective with variable rates. Prior to 1947 all contributions were lumped into a pool out of which benefits were paid.

How Does Our Present System Assign Taxes?

Alaska has what is described as a Quarterly Payroll Decline Experience Rating System. The objective of such a system is to assign the tax based on an employer's risk with unemployment as compared to other employers. This is in keeping with the insurance principle of pooling the risks and assigning a cost based on a degree of risk. Our system identifies the degree of risk through declines in the employer's quarterly payroll experience. The larger an employer's payroll decline as compared with the payroll declines of other employers, the larger rate he is assigned. Rates under the present system vary from 1.5 to 4.0 percent for employers and .3 to .9 percent for employees. This tax structure was actuarially designed in 1960 to produce a total average yield of 2.8 percent of total wages, or 3.5 percent of taxable wages. This average yield is made up of employer contributions of 2.9 percent and employee contributions of .6 percent of taxable wages. Taxable wages include wages up to \$7,200.

What Proportion of Total Payroll is Taxed and Does This Cause Regressive Taxation?

In 1960 when the last financial improvement was made to Alaska's tax structure, the base was raised from \$4,200 to \$7,200 and at that time almost 90 percent of total payroll was taxed. Since more and more workers have achieved annual incomes greater than \$7,200, the percent of wages taxed in 1970 fell to about 70 percent. The percent of wages taxed in 1977, the last year of our Actuarial Planning Period, is expected to be only 60 percent. One can easily see the widening gap between total and taxable payroll in Chart 4. This means, as wages increase, the tax burden is shifted from employers' who employ both high and low wage workers to primarily those employers' who employ low wage workers. Our tax structure has changed from one that was fairly equitable in 1960 to one in which each year a relatively higher rate of contributions are paid by low wage employers. For exactly the same reason that a tax structure with a limited tax base discriminates against the low wage employer, it also discriminates against the low wage worker. To further illustrate how the tax is regressive consider the following example:

Assume the case where the low and high wage employer pays the average contribution rate of 2.9 percent of taxable wages.

In 1960 the 2.9 tax to the high wage employer was equivalent to a tax of 2.6 percent of total wages, as taxable wages were equal to 88 percent of total wages. In 1970 2.1 percent of total wages were taxed as his taxable wages made up only 73 percent of total wages.

Yet the low wage employer, the majority of whose employees were paid less than \$7,200, paid a tax in 1960 of 2.9 percent of taxable wages and 2.8 percent of total wages. In 1970 the low wage employer continued to pay 2.9 percent of taxable wages which was equivalent to 2.6 percent of total wages (based on a taxable to total wage ratio of .91).

This tax is definitely regressive since the high wage employer paid .5 percent less over the period while the lower wage employer paid only .2 percent less.

Any tax which is not based on total wages discriminates against the low wage employer and employee, as each year a greater proportion of his wages are taxed. In other words, our present tax structure definitely results in regressive taxation which makes the employers' tax burdens unequal in relation to their payroll on the basis of which the tax is supposedly imposed.

Equal Taxation

To spread the costs equally to all participants in the economy, we would eliminate regressive taxation by taxing total wages so that the large wage earner is taxed at the same percentage of his wage as the low wage earner's wage. The same can be said for the low and high wage "employer". Would it be right for a \$10,000 a year worker, whose wages are taxed at 72 percent, to purchase \$50 worth of groceries for \$36; while the \$4,000 worker paid the "full amount"?

A tax structure which assigns equal rates to all employers would seem to cause employers to be less concerned about increases in benefits, since his rate would not go up if his payroll declined. However, he would easily recognize that the reserve multiple tax concept assigns a tax based on the fund's adequacy and that the fund's adequacy is dependent upon the amount of benefits paid. He recognizes, therefore, that the less adequate the fund is the higher his tax will be. An equal rate structure would cause him to be no more or less concerned about benefit payment than he is about his own profit.

PART V

BENEFIT COSTS FOR 1972 AND 1972-1977 ACTUARIAL PLANNING PERIOD

BENEFIT COSTS FOR 1972

AND

1972 - 1977 ACTUARIAL PLANNING PERIOD

An Unemployment Insurance fund must be appraised in light of potential liabilities. As a measure of potential liabilities, previous benefit costs along with careful consideration of the economic conditions which generated those high costs can be a good gauge. To realize relative changes, income, benefit costs, and reserves must be stated as percentages of total wages. The following sections explain our measure of adequacy, the reserve multiple, and generally how the rate for the 1.4 to 1.6 interval in our reserve multiple tax structure was derived.

Reserve Multiple - Measure of Adequacy

As noted in the financial section, we have designed a tax structure to produce a predetermined yield during the 1972 - 1977 Actuarial Planning Period to meet the expected benefit costs of our recommended benefit structure. This tax structure is also designed to build the fund up to an adequate level. This level, as suggested by the Federal Government as a guideline in considering adequacy of a State reserve fund in relation to potential recession costs is a reserve (as a percent of the latest twelve-months total wages) equal to 1.5 - 3.0 times the ratio of benefits to total wages in the highest twelve month period experienced since 1957. This minimum safe level for rate reduction would be achieved in Alaska when the reserve on September 30 as a percent of the twelve month total wages ending June 30 equals 1.5 times 4.33 percent, Alaska's highest benefit cost rate since 1957. Alaska's reserve multiple on September 30, 1970 was 1.24.

Balancing Income and Expense Over a Period of Time

Projected cost rates are made for 1972, the effective date of the Federal conforming and recommended State Legislation, and for the 1972 - 1977 Actuarial Planning Period. Projections were made under three assumed economic patterns and are expressed as averages for the 1972 - 1977 period. The projections under an estimated average insured unemployment rate of 8% for the 1972 - 1977 period were used to derive the rate for the 1.4 to 1.6 interval. The need to detail individual years is unnecessary, since interim fluctuations are automatically taken care of by averaging the cost factors. In so doing, the reserve multiple tax concept's basic objective of balancing income and expense over a period of time will be accomplished.

CALENDAR YEAR 1972

ESTIMATED ALASKA U. I. BENEFIT COSTS

TO CONFORM TO P. L. 91-373

<u>ECONOMIC PATTERN</u>	<u>I</u>	<u>II</u>	<u>III</u>
<u>INSURED UNEMPLOYMENT RATE (IUR)</u>	<u>7.0</u>	<u>8.0</u>	<u>9.0</u>
BENEFIT COST RATE AS PERCENT OF TOTAL WAGES			
P. L. 91-373			
Removal of \$20 Interstate Restriction	.143	.167	.194
Participation in Wage Combining	.040	.047	.054
Extended Benefit Program (50% State share)	<u>2/</u>	<u>.043</u>	<u>.053</u>
Total	.183	.257	.301
Current Law	<u>1.357</u>	<u>1.587</u>	<u>1.842</u>
Total	1.540	1.844	2.143
Recommended Benefit Improvements	<u>.683</u>	<u>.806</u>	<u>.911</u>
Total	2.223	2.650	3.054
AMOUNT OF BENEFIT COSTS (\$ MILLION) <u>1/</u>			
P. L. 91-373			
Removal of \$20 Interstate Restriction	\$1.15	\$1.34	\$1.55
Participation in Wage Combining	.32	.38	.43
Extended Benefit Program (50% State share)	<u>2/</u>	<u>.34</u>	<u>.42</u>
Total	1.47	2.06	2.41
Current Law	<u>10.87</u>	<u>12.71</u>	<u>14.76</u>
Total	\$12.34	\$14.77	\$17.17
Recommended Benefit Improvements	<u>5.47</u>	<u>6.46</u>	<u>7.30</u>
Total	\$17.81	\$21.23	\$24.47

1/ Based on estimated Calendar Year 1972 total covered wages of \$801,000,000.

2/ The Extended Benefit Program in 1972 would not likely trigger at a 7.0 IUR.

TAXES REQUIRED TO FINANCE RECOMMENDED BENEFIT IMPROVEMENTS
FOR THE 1972-1977 ACTUARIAL PLANNING PERIOD

I F

TAX RATE = COST RATE

THEN

Reserves at End of Period will Equal

Current Reserve	\$34.1 million
+ Interest on Reserve	<u>14.0</u>
	\$48.1

B U T

	<u>1970</u>	<u>1977</u>
Total Wages	\$650.0	\$1,105.4
Reserves	34.1	48.1
Reserve Percentage	5.25	4.35
Reserve Multiple (Divide by 4.33%).....	1.21	1.00

T H E R E F O R E

If We want to Maintain a RESERVE MULTIPLE EQUAL to 1.5,

\$ Reserves Must Increase To:

\$72 million ^{1/} by the end of 1977

H O W

TAX RATE MUST BE HIGHER THAN COST RATE

HOW MUCH HIGHER?

^{1/} $\frac{1977 \$ \text{ Reserve}}{1977 \text{ Total Wages}} \div \text{Highest Benefit Cost Rate} = \text{Minimum Adequate Reserve Multiple}$

OR

$\frac{\$ 72 \text{ Million}}{\$1,105.4 \text{ Million}} \div 4.33\% = 1.5$

GROWTH FACTOR TO MAINTAIN A RESERVE MULTIPLE OF 1.5
(Percent of Total Wages)

ECONOMIC PATTERN (Growth)	<u>Moderate</u>	<u>Intermediate</u>	<u>Rapid</u>
<u>Insured Unemployment Rate</u>	<u>9.0</u>	<u>8.0</u>	<u>7.0</u>
Growth Factor.....	.33	.51	.60
Less: Percentage from Interest.....	.27	.24	.23
Net Increment.....	.06	.27	.37

ESTIMATED TAX RATES

ECONOMIC PATTERN	<u>Moderate</u>	<u>Intermediate</u>	<u>Rapid</u>
<u>Insured Unemployment Rate</u>	<u>9.0</u>	<u>8.0</u>	<u>7.0</u>
Cost Rate.....	2.95	2.54	2.12
Net Increment.....	.06	.27	.37
Tax Rate.....	3.01	2.81	2.49

The 2.7 RATE was ASSIGNED to the
INTERVAL in the Tax Structure WHICH
CONTAINS the 1.5 RESERVE MULTIPLE

