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DEPUTY DIRECTOR

STATE OF HAWAIʻI
KA MOKUʻĀINA O HAWAIʻI
DEPARTMENT OF LABOR AND INDUSTRIAL RELATIONS
KA ʻOIHANA PONO LIMAHANA

February 21, 2025

To: The Honorable Kyle T. Yamashita, Chair,
The Honorable Jenna Takenouchi, Vice Chair, and
Members of the House Committee on Finance

Date: Friday, February 21, 2025
Time: 10:00 a.m.
Place: Conference Room 308, State Capitol

From: Jade T. Butay, Director
Department of Labor and Industrial Relations (DLIR)

Re: H.B. 202 HD1 RELATING TO THE ADEQUATE RESERVE FUND

I. OVERVIEW OF PROPOSED LEGISLATION

The **DLIR strongly supports** this measure that seeks to amend the definition of “adequate reserve fund” starting calendar year 2026 while preserving the exclusion for the COVID-19 Pandemic.

The "adequate reserve fund" will be calculated by multiplying the highest benefit cost rate from the past ten years (excluding June 2020–August 2021) by total employer remuneration from the last four calendar quarters, then applying a multiplier of one and one-quarter for calendar year 2026 and one and one-half for calendar year 2027 and thereafter.

II. CURRENT LAW

The Benefit Cost Rate (BCR) is the total benefits paid during a consecutive twelve-month period divided by wages for a twelve-month period.

The Adequate Reserve Fund is a benchmark that equals the highest BCR during the most recent ten years times total wages for the last completed fiscal year ending June 30. The calculation of the Adequate Reserve Fund is designed to ensure there are enough reserves in the Unemployment Compensation Trust Fund (UCTF) to pay Unemployment Insurance (UI) benefits.

The Adequate Reserve Fund is used as a measure of the solvency of the UCTF and to determine the UI tax schedule: the ratio of the Current Reserve divided by the Adequate Reserve determines which UI tax schedule is in effect for a calendar year (Current Reserve/Adequate Reserve).

Ratio = Current reserve/adequate reserve

Ratio CR/AR	Tax Schedule
1.69 +	A
1.3-1.69	B
1.0 to 1.29	C
0.80 to 0.99	D
0.60 to 0.79	E
0.40 to 0.59	F
0.20 to 0.39	G
< .20	H

An employer's state unemployment insurance tax rate is computed once a year based on the employer's reserve ratio and the tax schedule in effect for the year.

III. COMMENTS ON THE HOUSE BILL

The DLIR strongly supports this measure as it safeguards the health and long-term stability of the UCTF. The DLIR respectfully requests that the measure's defective date on page 4, line 8 be amended to take effect upon approval.

When §383-63 was originally drafted, guidance from the United States Department of Labor (U.S.DOL) was used to determine that the "one and one-half times" multiplier was the minimum amount needed to withstand a severe spell of unemployment at the time. However, in 2010 the multiplier was decreased to a factor of one, which negatively impacted the UCTF's reserve balance.

The COVID-19 Pandemic caused an unprecedented surge in unemployment across Hawaii, rapidly depleting the UCTF and forcing the State to borrow approximately $700 million from the USDOL. Informal analyses suggest that if the one and one-half multiplier had remained in place, the UCTF would not have been as negatively impacted as it was.

Throughout the COVID-19 Pandemic, the DLIR supported employers by advocating for and implementing measures that became Act 1 (SLH, 2021) and Act 281 (SLH, 2022). Act 281 amended §383-63 to exclude the BCR from June 2020 to August 2021 to prevent the Pandemic-related, anomalous outflow from severely impacting the Adequate Reserve Fund definition and employer taxes.[1] Both of these acts provided both immediate and sustained relief to employers.

Although the UCTF has since rebounded from the impacts of the COVID-19 Pandemic and the Maui Wildfires, restoring the original one and one-half multiplier is essential. The DLIR believes that this phased approach will strengthen the UCTF's financial resilience, ensuring that the UCTF is prepared for future economic crises, including to serve its purpose as an economic stabilizer during downturns, and protect Hawaii's workforce during unexpected hardships while minimizing the impact on employers.

[1] Effective for the calendar years 2023 through 2030, "adequate reserve fund" means an amount that is equal to the amount derived by multiplying the benefit cost rate that is the highest during the ten-year period ending on November 30 of each year by the total remuneration paid by all employers, with respect to all employment for which contributions are payable during the last four calendar quarters ending on June 30 of the same year, as reported on contribution reports filed on or before October 31 of the same year, but shall not include the benefit cost rate from June 2020 through August 2021.

TAX FOUNDATION OF HAWAII

735 Bishop Street, Suite 417 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: UNEMPLOYMENT, Amends Formula to Increase Adequate Reserve Fund Temporarily

BILL NUMBER: HB 202 HD 1

INTRODUCED BY: House Committee on Labor

EXECUTIVE SUMMARY: Amends the definition of "adequate reserve fund" for calendar years 2026 and thereafter.

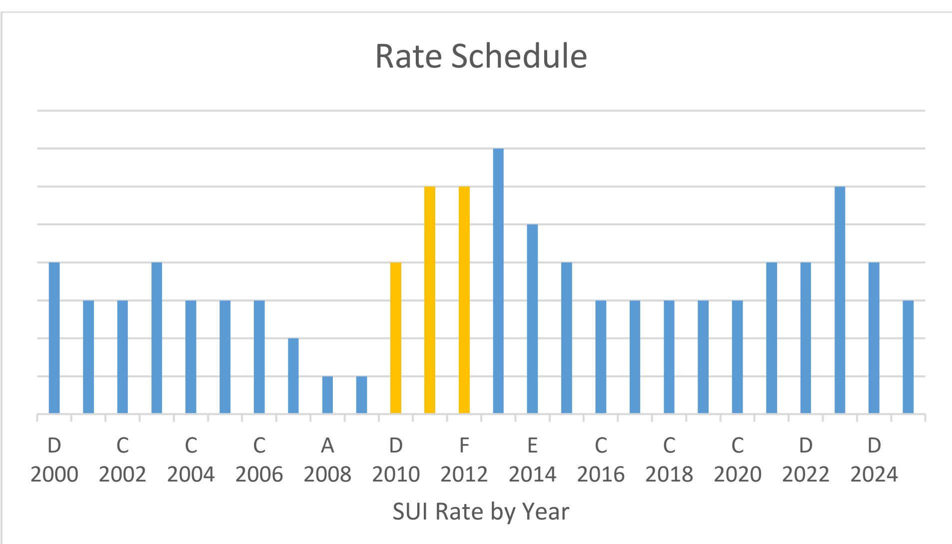
SYNOPSIS: Amends section 383-63, HRS, definition of "Adequate reserve fund" to mean an the amount that would be the adequate reserve fund under existing law, times

1) 125% for calendar years 2026; and
2) 150% for calendar years 2027 and thereafter.

EFFECTIVE DATE: January 1, 3000.

STAFF COMMENTS: State unemployment insurance (SUI) is largely funded by employers. Most employers are charged tax that depends on two things: the overall health of the fund into which SUI tax is collected, and the claims history of the employer. So, an employer with a long history of chargeable claims, for example, will pay more than others. Also, if there is lots of money built up in the fund then the tax rate goes down for everyone.

The health of the fund determines the proper tax rate schedule. The schedules are named after a letter of the alphabet, with A the least costly schedule and H the most expensive. The fund health is measured at the end of the year, and that measurement is used to set the rate for the following year. Here is a chart of the SUI rate schedule for the past 25 years:



Source: DLIR Reports compiled by Tax Foundation of Hawaii.

Although the Great Recession of 2008 and related events caused the fund to run out of money and we needed to borrow around $180 million from Uncle Sam, employers were not subjected to the dreaded Schedule H because our lawmakers passed special legislation to control the SUI rates and override the normal formulas for the years 2010 through 2012 (the orange bars in the diagram). That also happened for 2021, where Act 1, SLH 2021, set the rate at Schedule D for 2021 and 2022.

The change requested in this bill artificially increases tax rates by inflating the target for the reserve fund by 25% or 50% while, of course, the amount of money in the actual fund does not change.

To illustrate what happens if the bill takes effect, suppose the current unemployment reserve fund in Hawaii is $200 million (which is what it was in November 2022). Also suppose that the adequate reserve fund, calculated under existing law, is also $200 million. Under section 383-68(d), HRS, we would have a ratio of current to adequate reserve fund of 1.00 and employers would have a contribution rate schedule of C. That rate schedule is somewhat normal for us, as we had this schedule in effect for 11 of the past 25 years. That would correspond to a SUI tax for new employers (with a zero reserve ratio) of 2.4% of taxable wages.

If we are in the period 2026 through 2027, the adequate reserve fund is artificially raised to $250 million. That would make the ratio of current to adequate reserve fund drop to 0.80 and employers would have a contribution rate schedule of D. That would correspond to a SUI tax for new employers of 3.0% of taxable wages.

If we are in the period 2028 through 2030, the adequate reserve fund is artificially raised to $300 million. That would make the ratio of current to adequate reserve fund drop to 0.67, placing employers with a contribution rate schedule of E, and our new employer would receive a tax rate of 3.4% of taxable wages.

Is this really what we want?

Digested: 2/19/2025