Unemployment Insurance Trust Fund and Reed Act funds

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Unemployment insurance taxes, which are required for most employers, have two components – a state unemployment tax (SUTA) and a federal unemployment tax (FUTA).

Unemployment insurance taxes have two components

Unemployment Insurance Trust Fund

Under federal law, the state portion goes directly into the unemployment-insurance trust fund. The state trust fund and interest on deposits can be used only to pay benefits; the state has no flexibility on its use.

State unemployment tax may be used only for unemployment benefits

The Reed Act

The state also has access to federal unemployment-insurance funds through the Reed Act Account, which allows some flexibility and can be used for expenses other than benefits, provided the use is legislatively appropriated.

The Reed Act is a portion of the Employment Security Financing Act of 1954 that provides a mechanism for returning excess federal taxes to the state employment security agencies. The FUTA tax is levied on employers to finance the administrative costs of the unemployment-insurance and employment-service programs. It also provides reserve funds for possible extended-benefit programs and a loan fund for states that deplete their individual benefit accounts. When the national accounts for administration, extended benefits and state loans reach their statutory caps, the excess is distributed to the states – a Reed Act distribution.

Excess federal unemployment taxes go into Reed Act Account, which has more flexibility

Reed Act distributions

Historically, when the statutory caps were close to being reached, the caps were simply increased by Congress in order to keep the funds in the federal accounts, making the federal deficit appear to be smaller.

In 2002, the Temporary Extended Unemployment Compensation Act (TEUCA) directed a $8 billion Reed Act distribution to the states (double what would have been warranted under normal circumstances). The Washington state allocation was $167 million and was transferred to the state's Unemployment Insurance Trust Fund.

Permissible uses of Reed Act money

The state legislature must appropriate Reed Act funds. The states have some latitude in the use of a Reed Act distribution, with limited federal oversight. The funds can be used to pay unemployment benefits, to cover unemployment-insurance or employment-service administrative costs and, in some circumstances, can be used as a revolving fund for major infrastructure investments, such as data-processing installations. Reed Act expenditures for qualifying infrastructure investments can be amortized through federal grants, without interest. These amortization payments are re-deposited into the state's Reed Act account and restore a balance that can then be used again.

Only the principal balance can be appropriated. Interest earnings that accrue to the Unemployment Insurance Trust Fund from Reed Act funds can be used only for paying unemployment benefits. Every appropriation of funds for administrative purposes reduces the amount of the principal balance. Only the amortization of qualifying major infrastructure investments with federal funds, as explained above, can restore the principal.

Reed Act funds have no time limit. The state can simply leave the funds in the trust fund.

Risks of improper use of Reed Act funds

States must adhere to the requirements of the federal law. If a state law authorizes the use of Reed Act funds in violation of federal law, the Secretary of Labor can choose to:

- Take away the federal grant used by the state to administer the unemployment-insurance and employment-service programs – approximately $100 million per year.
- Withhold roughly $1 billion per year in federal tax credits from Washington employers.

Contacts

Sheryl Hutchison, communications director, 360-902-9289