STATE OF NEVADA
DEPARTMENT OF EMPLOYMENT, TRAINING AND REHABILITATION
EMPLOYMENT SECURITY COUNCIL MEETING

August 3, 2010

Live Meeting:
Legislative Building
401 S. Carson Street, Room 2135
Carson City, Nevada 89701

Video Conference to:
Grant Sawyer Building
555 E. Washington Ave., Room 4412
Las Vegas, Nevada 89101

Note: This meeting was also broadcast on the Internet at www.leg.state.nv.us.

Council Members Present
Paul Havas, Chair - Employers
Charles Billings * - Employees/Labor
Kathleen Johnson * - Public
Daniel Costella - Employees/Labor
Margaret Wittenberg * - Employers
David Garbarino - Employees/Labor
Paul Barton - Public
Ross Whitacre - Public
Michelle Carranza - Employers
(* Serving on the Board of Review/DETR)

Department of Employment, Training and Rehabilitation (DETR) Staff
Present in Carson City
Cynthia Jones, DETR Deputy Director/Employment Security Division (ESD) Administrator
J. Thomas Susich, Legal Counsel, ESD/DETR
Dave Schmidt, Bureau of Research & Analysis, DETR
Donna Clark, Chief, Unemployment Insurance Contributions (UIC), ESD/DETR
Kelly Karch, Deputy Administrator, ESD/DETR
Jered McDonald, Economist,, Research & Analysis, DETR
Jeffrey Frischmann, Chief, Field Direction & Management, ESD/DETR
Edward Lagomarsino, UIC/ESD/DETR
Flo Bedrosian, UIC/ESD/DETR
Joyce Golden, Administrative Office, ESD/DETR
Nathan Garnica, NTIC/ESD/DETR

Present in Las Vegas
Larry J. Mosley, Director, DETR
Mae Worthey, Public Information Officer, DETR
Art Martinez, ESD/DETR

Members of the Public, Media and Other Agencies
Cy Ryan, Las Vegas Sun, Capitol Press Room, Carson City/NV
Geoff Dorman, Nevada Appeal, Capitol Press Room, Carson City/NV
Tray Abney, Reno/Sparks Chamber of Commerce, Reno/NV
Buzz Harris, Nevada AGC, Reno/NV
Ray Bacon, Nevada Manufacturers Association
Sandra Chereb, Associated Press, Carson City, NV
Kris Holt, Nevada Business Connections, Carson City, NV
Veronica Meter, Las Vegas Chamber of Commerce, LV/NV
George Ross, Snell & Wilmer, Chamber of Commerce, LV/NV
Sam McMaregan. Snell & Wilmer, LV/NV
Carole Vilardo, NTA, LV/NV
Katherine Jacobi, Nevada Restaurant Association, LV/NV
Misty Grimmer, LV/NV
Bryan Wachter, RAN, LV/NV

Exhibits

Exhibit A - Attendance Record

Exhibit B - Agenda for the meeting/workshop

Exhibit C - Nevada’s Economy: A Review and Outlook

Exhibit D - Review of Unemployment Insurance Trust Fund

Exhibit E - Trust Fund Loans and Repayment Strategies

Exhibit F - Overview of the Unemployment Insurance Experience Rating Process

I. CALL TO ORDER AND WELCOME

Paul Havas, Chair of the Employment Security Council, called the meeting to order at 10:00 a.m. on August 3, 2010. Mr. Havas expressed his appreciation of those attending and welcomed all to the meeting. **Exhibit A is the attendance record** of all those present.

The Chairman of the Council introduced himself. I am Paul Havas, the Chairman of the Nevada Employment Security Council. Thank you members of the Council, public, and staff for your participation in today's informational Security Council meeting. It is common knowledge that the nation's and this state's economy has been in distress for the past couple of years. Nevada's historically high unemployment rate has resulted in unprecedented levels of benefit payments. As a result, the Unemployment Insurance Trust Fund, which only is used to pay benefits, was depleted in October of 2009. The purpose of today's meeting is to begin the discussion on how to establish a fair and equitable tax strategy to pay benefits, repay loans, and rebuild the Unemployment Insurance Trust Fund solvency in the future that takes into account the impact on Nevada's business community.
Exhibit B is the Meeting Agenda.

II. INTRODUCTION OF COUNCIL MEMBERS

At this juncture, I would like to introduce the Council members. Again, my name is Paul Havas. I represent employers as Chairman; Kathleen Johnson, Public and also serves as the Chairwoman on the Board of Review; Charles Billings, Employees/Labor and serves on the Board of Review; Margaret Wittenberg, Employers and serves on the Board of Review as well; David Garbarino, Employees/Labor; Ross Whitacre, Public; Paul Barton, Public; Michelle Carranza, Employers; and Daniel Costello, Employees/Labor.

The Council requests that the Employment Security Division Administrator, Cindy Jones, make some opening remarks to set the stage for today's meeting.

III. OPENING REMARKS

Cindy Jones, Deputy Director of the Dept. of Employment, Training & Rehabilitation (DETR) and Administrator of the Employment Security Division (ESD)

Thank you, Mr. Chairman. Good morning members of the Council, public, staff, and those watching on the Internet, as well. My name is Cindy Jones and I do serve as the Administrator of the Employment Security Division for the Department of Employment, Training and Rehabilitation and I am also an Ex-Officio member of the Employment Security Council and its Secretary in accordance with Nevada Revised Statute 612. At the request of the Employment Security Council Chair and Council members, today's meeting is being conducted as a precursor to the Rate Recommendation Regulation Workshop to be conducted in October. With the Trust Fund deficit situation there are extraordinary factors that will impact the rate setting recommendation.

Council members requested an early meeting so that they, and interested parties, are better prepared to provide a more informed input and recommendations at the Employment Security Council meeting in October. Please note that no action items are contained on today's agenda and no rate recommendation will be made today.

Ms. Jones asked Ms. Golden if proper notice of today's public meeting was given as required by NRS 233B.060 and if any written comments were received. To this Ms. Golden responded with "Yes, proper notice was given. We received on written comment from one small business in Sparks, Nevada, stating opposition to a tax increase and requested to maintain the contribution levels at the 2010 level".

Ms. Jones thanked Ms. Golden and continued to say that we did receive one public comment that suggested that we leave the tax rate schedule similar to that held in 2010 or keeping the average tax rate the same. As I had mentioned, the rate setting process will occur in October. In accordance with NRS 3, 612.320, the Council does provide that recommendation to the Administrator regarding the taxable rate schedule for the upcoming calendar year after the statutory solvency test occurs at the end of September.

Last year, the Council recommended that the average tax rate remain the same in 2010 as it was in 2009, in recognition of the financial distress the business community was experiencing as the result of the national recession that continues to hit Nevada particularly hard. There was recognition at that meeting, that delaying the tax increases towards regaining solvency would result in higher cost overall to the employer community in the long run, due to the interest costs that would be generated from borrowing from the federal government to continue to pay unemployment insurance benefits.

The presentations you are about to hear are intended to provide you with in depth topical information about the complicated task ahead. Please do keep in mind that all the numbers in the presentations are indeed preliminary and will be adjusted, based upon the official solvency test that is conducted at the end of September and other updated numbers, and presented at the October Council meeting and regulation workshop. For those viewing this meeting on the Internet, the PowerPoint presentations being made today are available on the Department's website at www.nvdetr.org. Towards the bottom of the right side, you'll find a section that says "click links" and under "public meetings" there is a section for today's meeting, where the PowerPoint presentations can be found.

The format that we hope to follow today is that, at the end of each topic, discussion will be open to the Council members to ask questions. In order to keep the meeting on course, we request that interested parties, questions, or comments be held to the public comment part of the agenda. At this time, I'll turn the meeting back over to the Chairman to introduce the next agenda items, thank you.

Mr. Havas thanked Ms. Jones and called upon Jered McDonald to provide an economic overview and projections.

IV. <u>ECONOMIC OVERVIEW AND PROJECTIONS</u>

Jered McDonald, Economist, Research and Analysis Bureau, DETR

Jered McDonald introduced himself and said he would be presenting a brief economic review and outlook that would set the stage for a UI Trust Fund update presented by Mr. David Schmidt, his colleague. For informational purposes, he will also present an array of potential strategies we may use to manage the fund moving forward. My presentation will include a, a review of the effects the recession has had on population unemployment and employment. I will also have a look at some demographics and kind of a look at how this recession compares to other recessions. It will also include a review of current trends to see how we're doing this year compared to last and finally I will provide DETR's employment and unemployment forecast.

Over the last forty years, Nevada's population grew significantly, grown by over five-fold rising from a mere 500,000 in 1970 to 2.5 million in 2009. For most of the period, Nevada was the fastest or one of the fastest growing States in the nation, as readily available economic opportunities drew thousands of new Nevadans to the state each year. Past recessions seemed to have little effect on Nevada's population growth. In fact, Nevada never lost population from one year to the next, at least on this graph from 1970 to current, but certainly much longer than that.

Of late, we've seen our rate of growth decline significantly as job prospects for new workers have disappeared, and we will likely lose population for the first this year, as workers leave the state to find jobs in other states. **<u>Exhibit C is Nevada's Economy: A Review and Outlook</u>**.

This graph pretty much tells the story of the recession and what's been happening of late. This is a comparison of Nevada's unemployment rate versus the nation's. As you can see, the rate for both grew substantially starting in 2008. In recent months though, Nevada's economy appears to have decoupled from the nation's, meaning we seem to be going in different directions. The national unemployment rate peaked at 10% in December and has leveled out over the first six months of the year. Nevada's rate on the other hand continues to rise. In May, we reached 14% unemployment surpassing Michigan as the highest in the nation.

A lot of states in the nation have seen improvement and their rates have actually declined, and that has partly to do why we've reached the top. California, for instance, their rate has declined as has Michigan's. Here we can see how the unemployment rate reacted to the last four recessions. Nevada reached a new all-time monthly high last year in May surpassing the previous high of 10.7% set in the recession of the early 1980s. Looking at it from an annual perspective, the highest unemployment rate occurred in 1982 at 9.9%. We're currently at 13.8% through June. In recent months, we've been able to develop some new information that we haven't had in the past that allows us to analyze the effects the recession has had on some demographic groups within the state; not as much as we would like, but certainly more than we've had, so that's good.

Here we can see the unemployment rate by gender (page 6 of Exhibit C). Given the effect the recession has had on the construction industry in particular, a traditionally male-dominated sector, it's not surprising to see the male rate has significantly outpaced the female rate in this recession. It's currently at over four percentage points higher.

Here's a look at unemployment rate by age group (pg 7). Most age groups are running in the 10 to 12% range. Obviously, the recession is hitting younger workers harder than other groups with an unemployment rate approaching 24%. We suspect older, experienced workers are taking jobs traditionally filled by younger, inexperienced workers. This trend provides serious long term ramifications for this age group over the course of their working years. Younger workers are losing out on the opportunity to gain valuable work skills; simple things, things we might take for granted such as showing up to work on time. I know I certainly learned my lesson the hard way on that. Also learning how to conduct one's self in a professional setting and really just a lot of the responsibilities you gain through, you know, your first couple of jobs. Though all age groups will struggle to overcome this recession, it may be more difficult for this group moving forward.

Switching over from unemployment to employment, you can see Nevada's employment base has grown significantly over time almost by an exponential rate, especially in the '90s and 2000s. You can also see that, in past recessions, we suffered little job loss. That's obviously changed with this recession. Employment peaked three years ago at about 1.3 million in May 2007. Since that point, we have lost over 180,000 jobs, or 17%.

This graph shows the Peak-to-Trough for the four most recent recessions (pg/9). It compares the length and months and job loss measured from an employment peak. As you can see, the depth and breadth of this recession is longer and deeper than anything we've seen in the last forty years. The recession of 2001, the green line, and 1991, the gray line, were mere blips on the radar compared to what we've seen now. Even the recession of the early '80s, previously Nevada's worst, had reached its previous employment peak in just thirty months. At thirty-eight months and counting, the current recession may now just be reaching bottom and will likely take years to gain all those jobs back.

Here's a similar graph (pg 10) showing how Nevada's largest industries have fared in the recession. Construction has been in recession the longest having peaked four years ago in June 2006. With the loss of over 50% of its employment base, it has also lost the most jobs. Most of the other industries appear to be reaching a trough, but they too have lost significant proportions of their employment base.

Here's a look (pg 11) at how these industries have fared in the last three years, the red columns versus the previous ten years in blue. As you can see, most industries have lost a large proportion of the jobs gained in the previous ten year period. Construction has actually lost more jobs in the last three than it gained in the previous ten year period from 1997 to 2007. Construction industry employment is currently at a level not seen since 1995. Leisure and hospitality has lost roughly half of the jobs it gained in the previous ten year period, while the other two, professional and business services and transportation and utilities, have lost over 20,000 each.

Switching over to a more current perspective, you can see that unemployment is higher in all regions of the state this year compared to last. As a lagging indicator, this is somewhat expected. This also means that unemployment will remain elevated for some time even after the recovery begins.

Las Vegas, with a June rate of 14.5% unemployment, currently has the highest rate of all metropolitan areas in the nation with a population of a million or more. The next highest is in nearby Riverside/San Bernardino area of California and, beyond that, Detroit, Michigan. Here's a snapshot look at unemployment rates by county, these are current and for June. Over the year rates are up in all counties. I have these shaded by an unofficial region or type. You can kind of see that generally unemployment rates are lower in the northeast mining region of the state, while rates are higher in the metropolitan or urban and surrounding areas of the state.

On a slightly more positive note, we are still losing jobs, but we are losing them at a slower rate this year compared to last. Over the year (pg 15), percentage decline is moderating in all regions. Last year through June, we were losing jobs at a nearly 9% clip compared to roughly 4% this year. So, job loss is moderating, which is a good thing. The same goes for the state's largest industries. Job losses are moderating this year compared to last. All except construction are losing less than 5% over the year. Construction is losing just slightly less this year on a percentage basis compared to last, but it's still losing jobs in extremely high rate. That was a brief review of the recession's impacts and current economic situation.

I will be now moving to the forecast portion of my presentation. At DETR, we base our projections on a number of inputs, including but not limited to, the mix of industries we have in our state. We look at all these industries and how they perform historically and how they may perform going forward under varying alternatives, economic alternatives.

In this chart (pg 17), I have a comparison of the industry mix for the nation compared to Nevada. The mix reveals a lot about how we got to where we are and where we may expect going forward. This recession has hit Nevada relatively hard, due in large part to the state's reliance on consumer's discretionary income. With over a quarter of the state's economy based on leisure and hospitality, Nevada was particularly hard hit in this recession. Some industries are inherently more stable than others such as educational and health services. This is really the only industry sector in the state that has grown through the recession, but its proportion in Nevada is roughly half that of the national average. This, too, likely played some role in Nevada's performance during this recession.

To see how Nevada's mix of industries have changed over the years and to give us an idea of what we may expect going forward, here's a look at how the industry mix has changed in Nevada over a ten year period (pg 18). This is a snapshot of 1999 versus 2009, and certainly we all know the state has changed a lot. There is certainly a lot more people but, by in large part, we didn't see a whole lot of change in our industry mix. We saw leisure and hospitality decline by four-tenths of a percent and others increase slightly. Most notably professional and business services and education and health services, each increased by two percentage points, but otherwise not a whole lot of change. Going forward, at least in the short term, in say two to five years, Nevada will continue to rely heavily on a consumer-driven economy for jobs and growth. Unfortunately, consumers are still in no position to increase their disposable income spending. Given household debt loads, wealth deterioration, and job uncertainty, it will likely take years for spending to return to pre-recession levels. Given that, here's our forecast for unemployment in Nevada.

Our rate has been increasing at about two to three percentage points per month this year. We expect the rate to creep up and top out in the fourth quarter of this year and then slowly decline in the years ahead. Though the rate will peak, this year, we expect the average annual rate to be slightly higher next year. We don't expect the rate to fall into single digits until 2014.

Here's a look at our current employment forecast. This is actually from January. We are working on a new set of projections that we will have available at the October meeting. These projections are based on employment covered under the Unemployment Insurance System, so this is actual employment reported to the Employment Security Division by Nevada's employers. This forecast is actually holding up pretty well so far. Through the first quarter, actual covered employment is down 5.5%, three times better than our forecasted 5.8%. Regardless of this positive reading, Nevada's employment outlook is still pretty weak. We expect continued job losses through 2011 and will not see annual over-the-year growth until 2012.

To wrap up, I would like to spend just a moment talking about Nevada's two traditional growth industries: leisure and hospitality and construction. Both have been and will continue to be important drivers of growth once the recovery begins. We see the leisure and hospitality industry bottoming out next year and proceeding to grow at a slow rate. Beyond the forecast period, growth will depend on the habits of the industry's customers. At this point, it is uncertain as to when customers will return at pre-recession levels and what level of spending they will bring once they do return.

As for construction, the industry was the first to go into recession and has fallen the furthest, but it too will be a vital component of growth in Nevada's economic recovery. Unfortunately, the near term outlook is not too promising. New home construction appears to have a ways to go before recovery takes hold, and with new resort construction at a standstill and the commercial and industrial sector seeing record vacancy rates, there will be little demand for new development through 2012.

So, in conclusion, Nevada's economy will remain weak and require a robust national recovery to see strong economic growth. Unfortunately, the strength of the national recovery is looking a little fragile or at least uncertain at this point. The Federal Reserve recently revised its forecast for GDP growth next year. The Central Bank believes the economy will grow in the 3 to 3.5% range this year versus its prior forecast of 3.2 to 3.7. They also revised down GDP growth in 2011 now seen at 3.5 to 4%, down from 3.4 to 4.5, so that's a half point decrease in their forecast which is pretty significant. At this level, a national jobs recovery will come slowly and the unemployment rate will decline at a slower rate than previously estimated. This tells us that Nevada's recovery will take significantly longer than in past recessions. We may not see employment return to pre-recession levels until sometime late this decade. Mr. McDonald concluded his presentation.

Chairman Havas opened up the meeting for a few questions from the Council members.

Someone asked how close the projections were last year. The person asked if DETR was right on, the person remembered it was going to be high, but actually it was much lower.

Mr. McDonald responded that he thought it was right around 9%, so DETR was pretty close on that. He said that initially they were slow to pick up the downturn since it was like nothing they had ever seen, they did start to pick it up about last September or so.

Another person wanted to know if Nevada has many out-of-state construction workers or have they moved away.

Mr. McDonald said that over the last ten years we had a lot move into the state, but construction moves a lot. It is very cyclically. It moves a lot when this business cycle goes up and down, but construction workers are used to moving from job to job. He suspects that a lot of those people that moved here over the last fifteen years probably already left.

Someone spoke up and said that we they hear about the expansion of projects in Las Vegas and some of those are doing fairly well. But it appears that the actual situation is better than the way Mr. McDonald characterized it, but the numbers do not reflect it.

Mr. McDonald responded and said that we just do not see a lot of growth. Housing, those mega resorts that hire up to 4,000 to 8,000 construction workers, we do not have that anymore. City Center wrapped up last year. There is one smaller one that is wrapping up this year, beyond that, we do not see any other big developments.

Council member Ross Whitacre spoke up and said that perhaps he missed it in hearing McDonald's presentation, but talking about employed, just talking about small businesses and employers, do you have any numbers on the number of businesses that are no longer with us as a result of the recession?

Mr. McDonald answered that he did not have any numbers with him, but he knows that the actual count of businesses paying into unemployment insurance has declined. We actually have fewer employers now that we did. He would do some more analysis and break it down as to smaller or larger businesses for the next meeting. Mr. Whitacre thought that would be a good idea.

Council member Carranza asked about slide number 17 and number 18. Do we have any theories as to why we really have not seen major changes in these percentages. Mr. McDonald felt that over the last ten years we saw phenomenal job growth in leisure and hospitality and because of that did not see the need to really expand our industry base beyond what we already had.

V. <u>REVIEW OF UNEMPLOYMENT INSURANCE TRUST FUND</u>

David Schmidt, Economist, Research and Analysis Bureau, DETR

David Schmidt introduced himself and began his presentation. I'm here today to give you an overview of the current state of the UI Trust Fund, provide some background with respect to the mechanisms and costs of borrowing and provide you with some preliminary strategies that the Council may consider as we approach the Employment Security Council meeting this October.

The Unemployment Insurance Program is a means of economic stabilization that was instituted following the Great Depression. This program does go through some macro-economic and micro-economic effects. In the macro-economy, it helps by providing additional benefits to people who have lost their incomes which helps to cushion the fall in demand in the economy at large. In the micro-economy, it helps by providing benefits to these workers which helps them to maintain their attachment to the local workforce and assist them with the transition to new employment. **Exhibit D is the Review of the UI Trust Fund.**

The Unemployment Insurance Program is funded counter-cyclically, which means we try to build reserves during good economic times, to help energize and feed those back into the economy during recessions. The current recession is like nothing Nevada's experienced in the history of the UI Program, which has been around since the late 1930s. The next few slides will provide you with some national perspective and then I will focus on what has been happening in Nevada. The next three slides in particular (pgs. 5-7) show the solvency of the fifty states as is measured by the average high cost multiple. This is a federally recommended solvency measure, where a level of 1.0 represents having a year's worth of benefits in reserve in the Trust Fund. This is based on the average payouts experienced during the three prior recessions. So, it tries to give some idea of what you might expect to need to pay out during a recession. This is from December 2007 when the recession started.

You can see that seventeen states, including Nevada, had a multiple of at least 1.0. There were twelve states that were in the middle range of 0.5 to 1.0 and twenty-one states began the recession with a solvency level of below 0.5. By December 2008 not an awful lot has changed, because the recession really got worse in the late part of 2008 and early 2009. A few states were hit harder, including Nevada, Arizona and Florida, states that were hit unusually hard by the housing cycle that we've seen. You can see that Nevada, Arizona and Florida, which did have multiples of 1.0 or greater, have fallen down into that middle range by the end of 2008. But when we switch to 2009, you can see that, nationally, solvency is falling pretty much everywhere.

Nevada, Arizona and Florida have all dropped down below 0.5 by the end of 2009. In fact, Nevada and Florida were borrowing by that point and Arizona began borrowing in March 2010. Only six states began the recession with a multiple of over 1.0 and since then fell into this red category of below 0.5. This helps show that even though seventeen states had multiples of 1.0 or greater, the recession has been felt a little bit more sharply in some states than others.

As of July 27th, this shows you the states that have had to borrow money at some point during the recession in order to pay unemployment benefits. Because revenue tends to flow kind of seasonally through the Trust Fund, some of the states have been able to at least temporarily repay their loans including New Hampshire, South Dakota, and Tennessee. However, their repayment has probably not been very strong and it remains to be seen through the rest of this year whether or not they'll have to borrow again. Nevada's currently in that category of having borrowed between $100 and $500 million. All three of those states that I mentioned earlier, Florida, Nevada and Arizona, I mean, see, Florida being a very large state, has already borrowed over a billion dollars.

Arizona and Nevada are both still under $500 million and borrowing, despite the impact that they've had in their housing markets, in part because, they all had solvent Trust Funds heading into the recession (pg 8). Because of falling solvency nationwide, several states have taken measures to try to restore solvency in their Trust Funds, or at least mitigate the impact. Twenty-seven states have increased their unemployment insurance tax rates or were scheduled to as of January 12th. Six states, legislatively, increased their taxable wage base. Three states revised their tax schedule triggers, which is an effective tax rate increase. Two states imposed a supplemental solvency tax. Two states increased taxes on employers with poor experience ratings and four states had frozen or reduced unemployment benefits. Some states had a combination of these (pg 9). So, overall, thirty-four states were expected to experience tax increases and/or benefit freezes this year.

One thing not included on this chart is, states with an indexed taxable wage base, which is something that Nevada has, because this is something that just gets revised automatically and isn't necessarily in response to any changes in the solvency of the Trust Fund. This is a slide that we presented at the Employment Security Council meeting last year. I think it's good to remind ourselves of where we were when we entered the recession. I would say that Nevada was reasonably prepared for the recession. In the quarter that the recession began, Nevada had the 18th strongest Trust Fund as measured by the average high cost multiple (pg 10). An average high cost multiple of 1.02 and a state solvency multiple of 1.47, that's calculated according to NRS 612.550.

This chart shows you the unemployment rate in various states when borrowing began (pg 11). You can see that two states began to borrow with an unemployment rate of less than 5%. Most states began their borrowing when they had an unemployment rate of between 6 and 11% and Nevada, because we've had a very high unemployment rate, we have been hit very hard by this recession, we managed to make it to an unemployment rate of I believe 13.2% as was the announced rate when we began borrowing last October, and this helps show the magnitude of the blow that Nevada's Trust Fund was able to sustain before we began borrowing in order to pay benefits.

Since October, this table (pg 12) shows you how much we've borrowed each month. As I said before, this is very seasonal, because of the way that revenues come into the Trust Fund and, because revenues or benefits, tend to get paid out even more during the winter months, especially the first quarter of the year. Revenues coming in during the first quarter are at their lowest during the year and benefits going out are the highest, so you can see from January to March, we borrowed significantly more than we did from April through June, April through June being the highest revenue quarter generally during the year.

This slide (pg 13) shows you the ten year, just sort of high level view of revenue coming into the system and benefits being paid out and the overall balance of the Trust Fund during those times. You can see that, from 2007 to 2009, revenue has declined slightly from about $400 million to a little over $300 million. But, over those same two years, unemployment benefit payments have gone from about $300 million to over a billion dollars in 2009. There's been a significant hit to the Trust Fund and it's important to note that the benefits being paid out here from the Trust Fund, this is only the first twenty-six weeks of benefits.

The federally paid extensions that were recently reauthorized by Congress and have been in place in one form or another since July of 2008, aren't paid out from the Trust Fund. Those are completely federally paid so that billion dollars in benefits, is just what we've had to pay out through the Trust Fund through revenues that we've taken in and through borrowing. This has definitely been, like I said before, unprecedented activity paying out over a billion dollars in benefits last year. This has also been the longest recession since the Nevada UI System was created over about two years, since December 2007.

A lot of recessions have been much shorter in recent years, less than a year in duration. Also, sort of reflecting the stress that the national economy's facing, that Congress would authorize up to seventy-three weeks worth of additional benefits in total; this is significantly more than they've had during previous recessions. This table (pg 15) shows initial claims, which is, people filing for new unemployment benefits. It's a way of looking at people entering into the UI System. You can see that activity has peaked in early 2009 and has been declining since then; down from over 30,000 to about 22,000 in the most recent months. But, even though we're declining, if you look across, the level that we're currently at, is comparable to where we were in the worst months following 9/11, when airlines were shutting down and there was a lot of worry about, are people going to travel, are they going to be coming back to Las Vegas.

So, though we've been declining for about a year and a half in our level of new claims, we've only now declined to the point that we were at during the worst part of the 2001 recession. For comparison purposes (pg 16), in June of 2010, our most recent number is that there were 193,000 people unemployed in the state. For comparison, in October 2001, which is the peak month in initial claims there, there were about 66,000 people unemployed. This shows you, since January of 2008, people who are unemployed, which is the red line on top, and people who are receiving unemployment benefits or filing unemployment insurance claims.

Of the blue part at the bottom of this graph represents regular unemployment claims, which is that first twenty-six weeks that we have to pay for through state taxes and the Trust Fund and the gray and light blue areas represent those federally paid extensions. It dips a little bit more sharply toward the end of that graph, in part because of the fact that there weren't, that the program expired temporarily in June of this year, so we would expect that to go back up. But, you can see there's a gap between the total number of people who are unemployed and the people who are receiving unemployment benefits, and this is people who are either not eligible or just not filing for unemployment insurance claims for one reason or another.

Going forward (pg 17), we have a significant shortfall in the Unemployment Insurance System, so we need a strategy that will help to pay benefits in the short term, repay loans as we move forward, and eventually restore solvency to the Trust Fund, because there will be recessions again in the future. This can also take into account related considerations, like the impact on employers for unemployment insurance taxes and the counter-cyclical nature of the UI program.

Just a little factoid: from 1945 to 2001, the average time between recessions has been 67 months, or about 5½ years. Recently, we've gone much longer. We had recession at about 1991-2001, so we had about ten years between recessions there; about ten years from the early '80s to the early '90s and then about six years, from 2001 to the beginning of the recession in 2007.

This table (pg 18) shows you the last four recessions before the current one and the tax rates that were in effect during the years of the recession and then the year that taxes peaked following that recession. In 2001, you can see the tax rates during the recession on an average basis, were 1.29% and then peaked in 2004 at 1.38%. In 1991, taxes during the recession were .99% and then peaked in 1993 at 1.55%. It's interesting to note: in 1974, there were actually a couple of recessions that were back to back. There was one in about 1971 and another in about 1974.

Prior to both of those recessions, the tax rate was 1.61%, which isn't on the table here. But, you can see that by 1976, the tax rate had peaked at 3.22%, which shows that the tax rate effectively doubled from that time to help repay the benefits that were paid out during that time. Also, the 1974 recession is the only time in Nevada's history that we've had to borrow in order to pay unemployment benefits.

This next table or chart (pg 19) rather, is one you're going to see again, so I will try to make sure you understand what's going on with it. In it, we show you the average tax rate that was in effect from 1950 to the present, and we also showed the benefit cost rate. This is the tax rate that would be necessary to pay benefits during that one year. It essentially takes benefits that are being paid out and divides it by total taxable wages in the state. When the orange line is above the blue line, these are times when the Trust Fund is going down or we're borrowing in order to pay benefits. When the blue line is above the orange line, this is when revenues are exceeding benefits and the Trust Fund is being built up. You can see that the current situation is that the benefit cost rate has gone through the roof.

When we are paying out a billion dollars in benefit payments a year, that's a pretty big number. The further above or the larger the gap between those lines, the faster the building up of the Trust Fund or the borrowing that's taking place. One other thing to note here: as you can see, is that the tax rate we have right now, has been fairly low and fairly stable for about twenty years. This is in part a reflection of the great economic growth and relevant stability that we've enjoyed in the state during that time.

Now I would like to take a look at the federal loan process (pg 21). This gives you some idea of what and of how we borrow and what the costs are. If a state's Unemployment Insurance Trust Fund is insufficient to pay benefits, states may borrow from the federal unemployment account. This borrowing is outlined in Title 12 of the Social Security Act, so we often refer to it as Title 12 loans. These loans are interest bearing and the interest rate is set, based on interest that's earned on positive Trust Fund balances during the prior year. One of the things that's important to keep in mind as we look at the cost of borrowing is, the difference between federal unemployment taxes or FUTA and state unemployment taxes or SUTA.

This table (pg 22) compares some of the differences between these. Federal unemployment taxes are paid on a fixed wage basis, $7,000. These are paid directly to the federal government through the IRS, Form 940. This in part, funds federal and state unemployment insurance administration programs and it also funds the federal unemployment account, which is where we draw those Title 12 loans from. This is a fixed tax rate of 6.2%. However, employers generally enjoy a 5.4% credit toward that tax rate, reducing the effective tax to 0.8% or about $56 per employee per year. In contrast, the state unemployment tax is on an index wage base in Nevada.

In 2010, the wage base is the first $27,000 of an employee's wages. In 2011, that's actually going to decline to $26,600 because, this is set by a formula that compares it to average wages in the prior year and average wages in Nevada declined slightly from 2008 to 2009, so that wage base and the maximum benefit payment will both be declining. These taxes are paid to Nevada.

They can only be used to pay unemployment benefits or the principal of loans that are made to paid unemployment benefits. All of these taxes turn into unemployment benefits essentially or go right into the Trust Fund to pay benefits. These are only used, again, for the first twenty-six weeks of benefits. This doesn't go towards those federally paid extensions and this average rate is set each year by regulation, it's currently 1.33% on average, though the effective tax rates on actual employers can range from 0.25% to 5.4%.

If a state uses Title 12 loans (pg 23) in order to pay benefits and has outstanding loans after two years, the federal government begins to reduce that FUTA credit, the 5.4% that I mentioned on the previous slide. Effectively, this increases the federal unemployment tax that's paid by employers. The longer the state is borrowing, the steeper this credit reduction becomes and all revenue that's generated by the increased portion of the FUTA tax, that credit offset, is applied directly toward the outstanding loan balance in that state.

On the second consecutive January 1st with outstanding loans (pg 25), the credit to employers is reduced by 0.3% or about $21 per employee. This credit is reduced by an additional 0.3% each subsequent year so that'll go from .3, .6, .9 and, essentially, an extra $21 per employee per year. In addition to this cost, there's an additional reduction that can get added to this that begins in the fifth year of borrowing.

On the fifth consecutive January 1st with outstanding loans, what's known as the BCR add-on is applied. This takes the higher of either 2.7% or the five-year average benefit cost ratio, which is, essentially, that orange line from the charts I was showing you earlier, but a five-year average of that, and then it subtracts from the larger of those two numbers the state's current average tax or the state's average tax rate in the prior year. In the fifth year of projected borrowing, what we're looking at right now would be 2014, the projected benefit cost ratio we're looking at right now is 3.9% for a five-year average. So, as an example of how this would be calculated, you would take 3.9% minus the 2013 average UI tax rate. If we left tax rates unchanged, this would be 3.9% minus 1.3% which would be 2.6%. The FUTA credit in addition to that 0.3% per year increase, would then be reduced by an additional 2.6% on top of that. It's important to note though, that the BCR add-on here is directly related to tax rates in the prior year, which means that it is a controllable thing. If tax rates are closer to the benefit cost rate, this add-on will be smaller and the reduction in employers' federal taxes would be proportionately smaller as well.

This table (pg 26) shows you the total FUTA credit offset calculations that we would be facing. The tax rate that I used for the sake of illustration here is just 1.3%, which is where we're currently at. In the first column, you can see the year and then the base reduction of 0.3% per year. The next shows you the five-year average benefit cost rate and then the tax rate and the BCR add-on, which is the higher of either 2.7% or that five-year benefit cost rate. So, if you look at 2016, when the five-year benefit cost rate falls to 2.6, the BCR add-on from that point forward would be 1.4% or 2.7% minus 1.3%.

The total FUTA offset credit reduction is the total of the BCR add-on and the base reduction. So, without any changes, when that BCR add-on kicks in, you can see, from 2013 to 2014, the credit offset jumps from 0.9% to 3.8% or about from $63 per employee to $266 per employee. The last column shows you the estimated total principal reduction that would take place each year, based on those offset federal tax credits. It is possible to cap the reductions in the FUTA offsets. These essentially can be capped if the state is making what the federal government would consider adequate progress towards restoring Trust Fund solvency. The cap is the higher of 0.6% credit reduction or the prior year's credit reduction. So, if you can't cap it at 0.3%, it has to rise to at least 0.6% and it can't go lower, you can only stop the advancing of it.

The four benchmarks that the state must meet in order to achieve this credit reduction are, that the state cannot take any action during the prior year, which would result in a reduction of the state's unemployment tax effort. Essentially, the state can't cut its unemployment insurance taxes. No state action can be taken during the prior year, which would be expected to result in a net decrease in the solvency of the state Unemployment Insurance System. For example, this would be something like raising unemployment benefits, or expanding eligibility of unemployment benefits. It's important to note that these are state actions, things like in the increase in the taxable wage base or an increase in the maximum benefits, because those are automatically tied by formula to average wages in the state, these don't count as state actions.

Decisions being made by the Employment Security Council or the legislature on the other hand, would be something we're actively doing. Third, the state unemployment tax rate has to be greater than or equal to the five-year average benefit cost rate. Your tax rate has to be high enough to be paying benefits and maintaining solvency. And finally, the state's outstanding loans from the federal government have to be less than in the third prior year and this helps to show that your Trust Fund loans are decreasing, that you are making progress toward repaying those loans.

In addition to the FUTA offset credits, the Trust Fund balance does have interest that's charged. Interest on Title 12 loans is due on September 30th. Failure to pay this interest results in program decertification, which is a very bad thing. The FUTA rate would immediately become 6.2% for employers, so that would increase statewide employers' FUTA taxes by about $480 million. The state would immediately lose access to Title 12 loans, which we're currently using to pay unemployment benefits, and the state would lose all administrative UI funding, which is worth about $25 million a year. Decertification is a very bad thing. That's sort of the big stick that the feds use to make sure that programs stay in line.

Funds used to pay interest cannot come from state unemployment taxes. The tax rates that are discussed in the Employment Security Council here do not affect interest directly, that interest has to be raised from another source. Currently, the ARRA stimulus bill does provide the interest on Title 12 loans. It's deemed paid through December 31st of this year. So, interest will begin to accrue on January 1st of 2011 on whatever outstanding loans we have at that time. This interest is charged based on the interest that's earned on positive Trust Fund balances in other states.

The most recently announced interest rate was from January 2009, about 4.6%. There was no rate announced in 2010, because all states' interest was deemed paid and the tax rate which will be in effect beginning January 1st will affect the actual interest that's due, because the first set of tax payments from that tax rate will come in during the second quarter, we have to pay this interest at the end of the third quarter, so it'll affect our balance a little bit.

This table (pg 32) shows you in general, the total interest expense you might expect if the tax rate were to be immediately raised and then held at a variety of tax rates to show you the effect of increases in the tax rate on this interest expense. In general, the earlier you increase the tax rate, helps to reduce your immediate need for borrowing and then helps you to repay your loan sooner. Mr. Schmidt stopped at this point to see there were any questions from the Council on this portion of his presentation.

Chairman Havas asked if there were any questions from the members of the Council at this point.

One Council member addressed Chairman Havas and asked to make a comment of two. It is a very complex topic as we've seen just going through this FUTA offset credit reduction. Long story short is that the federal loans will be paid back one way or another and, if the state doesn't pay back the loans, the feds have a mechanism by which they force a repayment schedule, let's say, on Nevada's employer community by reducing the FUTA offset credit reduction or, in a sense, raising the federal unemployment insurance taxes. As you can see, it can be quite the complicated scenario or land to navigate because it is a very complex law. But, I appreciate David trying to simplify it as best as he could for us. He had to explain it to me a few hundred times before I even began to understand the complexity of this topic, but I just wanted to make those comments. I think Mr. Whitacre has a question.

Council member Ross Whitacre took the floor and said he had just a comment and did not know whether he was right or wrong, but it seems to him that this system that the Department of Labor and the feds have set up to get money back from the states is designed for shorter term recessions, where there's a good chance that the economy will recover in a shorter period of time and, as you go into counter-cyclical funding, the money will come in to repay these loans. Mr. Whitacre thinks Nevada definitely and probably most states in the country, are really going to find themselves in a bind here because the money is not coming in to repay these loans. Mr. Whitacre feels and thinks that in the end, as these FUTA reductions come into play, in looking at the dollar numbers, that it's going to cost employers. He thinks it is unfair to the employers throughout the country, and so in Nevada also.

Chairman Havas: And, in a related question that I have, how do you stabilize the FUTA offset when, in fact, it's not clear as to where we are at? As you stated, they have discretionary authority and that concerns me. How do you give and explore discretionary authority?

Mr. Schmidt explained that it is measured by some, those four sort of concrete guide posts that they've set out. The five-year average benefit cost rate is something that, because it looks at the prior year, you could set that out as sort of the target, this is where you were at.

It's intended that states are able to see what the target is, if they want to choose to meet it and those, as far as I'm aware, don't change.

One of the staff members spoke up. Mr. Chairman, if I might, David will be going through some more of those when we go into the next section where some of the strategies might address that. States in general, as Mr. Schmidt had talked about, approximately forty states are now expected to borrow about $70 billion in order to pay benefits during this recession and presentations I've seen from the federal level, it's a national issue. You are right Mr. Whitacre, that states across the nation aren't expected to regain solvency across the nation in its entirety in time for the next recession.

It remains unseen if there will be any action at the federal level to provide any relief to states, to put some sort of capping mechanism other than what's in currently, in statute, if there will be other interest-free periods. I can hope, but I don't see any legislation introduced at this point and one of the things that the Council and the employer community and all interested parties will have to decide as part of this is, do we want to adopt a strategy in the long run that allows us to cap the FUTA offset reduction or let the feds take care of it and have less on the state side. David will go into more of that as he goes into the next part of the presentation.

Someone wanted to know about page 23, as Mr. Schmidt referenced the two-year payback period. Where is Nevada at in that? Are we within the one-year, have we started on that time period?

Mr. Schmidt responded by saying that Nevada began borrowing in October of 2009, so January 1, 2010 was the first year in that sequence. We are about a year and a half into it. January 2011 will be the second year that will start that particular clock.

At this juncture Chairman Havas asked for a short 15 minute break before continuing with Mr. Schmidt's next presentation regarding interest repayment on federal loans among other things.

VI. <u>TRUST FUND LOANS AND REPAYMENT STRATEGIES</u>

David Schmidt, Economist, Research and Analysis Bureau, DETR

Mr. Schmidt noted that his next presentation would start on page 33 which says "*Repayment Strategies*" and could be found in **<u>Exhibit E, the Trust Fund Loans and Repayment Strategies</u>**.

Moving forward, there are some general points to consider. There are pretty much an infinite number of strategies that the Employment Security Council can consider. None of what's presented here, obviously, not what's decided in October can lock the Council into a future course of action. It does meet annually to look at the latest data, so changes can be made to this as you go forth. This is sort of for illustration purposes. Both the magnitude and timing of tax increases matter. The earlier you increase taxes, the less borrowing you have to do, while benefit payments are still high and the faster you can repay the Trust Fund or the loans for the Trust Fund and, again, all numbers here are preliminary.

We haven't finished our forecast for the Employment Security Council meeting. There are some numbers that do not come in until right before that meeting in October, so these are mostly for illustration purposes, to give you an idea of what happens with various tax scenarios. There are two different approaches that you can consider that I have laid out here. We have a flat rate scenario where the Council recommends a tax rate for say 2011, but then is intended to remain in place over a number of years. You can also have a ramped scenario where you say you want to increase the average tax rate by 0.5% per year over a course of several years to work up towards some higher target tax rate. There are pros and cons to both approaches.

With a flat rate, because you would generally have a higher tax rate sooner, this helps to minimize the interest expense that the state faces and helps the Trust Fund regain solvency sooner, but it also puts the impact for employers much sooner in the process. A ramped increase, on the other hand, delays that impact on employers, but because you're initially making slower progress toward repaying your loans and restoring solvency, that then raises your interest and FUTA offset expenses.

To sort of illustrate what I mean by flat rate and ramped rate, this chart (pg 37) just shows four flat rates with the current rate of 1.33% being the base there, 2%, 2.75% and 3.5%. And, then a ramped increase that sort of goes up steadily through those rates to show the tax rate changes over time in each of those scenarios. This revisits the previous chart showing the benefit cost rate and the average tax rate. This is sort of foundational for a lot of charts that are going to follow in the rest of this presentation.

This (pg 38) gives you an idea of where we expect the benefit cost rate each year to go through about 2016. We do expect benefit payments to come down significantly over time. They have begun to fall from 2000, in 2010 compared to 2009. Initial claim levels and weekly claim levels have been running, in recent weeks, about 30% below where they were a year ago. It was early this year that we stopped seeing year over year growth and moved into a trend of year over year decreases although, as I said earlier, we are at a very high level and we have a very long way to go before we go back to where we've been historically.

The first strategy I present here (pg 39) is the current average tax rate of 1.33% and that shows what would happen if we just left the tax rate where it is through at least 2020. Under this scenario, it shifts a large amount of the burden for loan repayments to FUTA offsets. At the very bottom of the table, it shows that the expected loan repayment that would come from FUTA, would be about 62% of the total peak borrowing.

Under this scenario, the loans still haven't been repaid by the end of 2020, because of the high benefit costs that we're seeing in early years. Here we wouldn't expect maximum borrowing even to occur until about 2015, when benefit costs finally fall back to where they were and even then that's when we just start to repay the loans from the state unemployment tax side. This would have the highest FUTA reduction of all of these strategies of 4.1% in 2020 and probably increasing beyond that. That would be a cost per employee of $284 for that FUTA costs by the time it hits 4.1% and we would expect the maximum borrowing to pass $2 billion in 2015.

This chart (pg 40) illustrates that tax rate and you can see when the blue line extended forward crosses the orange line as we mentioned before, that's the point when you finally start to either build the Trust Fund or, in this case, repay loans. And, so maximum borrowing, in this chart, will occur when the tax rate line crosses the benefit cost rate line and these can be a little bit repetitive.

The next strategy has a flat rate of 2.0% (pg 41). You can see here that the maximum FUTA reduction would fall from 4.1 to 3.1%. The total loan repayment from FUTA would be about 55%. It still puts the majority of that repayment on the federal side instead of the state side. We would expect maximum borrowing in 2014 under this scenario and actually repay the Trust Fund loans in about 2019. In this scenario, none of the years experience that FUTA credit offset the reduction cap.

In early years, the tax rate is simply too low and, in later years, the tax rate is still below the falling level of that five year average benefit cost rate, so we never actually achieve those FUTA caps until the year when loans are actually repaid and it becomes a moot point. We expect, in this case, the per employee FUTA costs, when it peaks, would be about $220 per employee with total interests falling to a little under $400 million total over the course of the time it would take to repay the loans. And again, we see the same chart and maximum borrowing occurs when the two cross (pg 42). This is still delayed a few years because you're mostly waiting for benefit costs to fall instead of increasing the tax rate to try to catch up sooner.

The next strategy (pg 43), 2.75%, you'd expect a maximum FUTA reduction of about 2.4%, the cost per employee of $167. In this scenario, loans are repaid in 2015 and we would expect about 36% of the loan repayment to come from FUTA. As the tax rate increases, an increasing share of those repaid loans comes from the state funds instead of federal funds. Also, in this case, because tax rates are going up sooner, we'd only expect borrowing to peak at about $1.11.2 billion instead of the $2 billion we saw with the 1.33 rate, and interest has now fallen to about $230 million total. Again, you can see that illustrated, the higher the tax rate goes, the sooner the point of maximum borrowing. In this case, 2013, because you're sort of increasing the tax rate closer to that declining benefit cost rate.

The next slide (pg 45) is 3.5%. Here, we'd expect a maximum FUTA reduction of 1.6%. We actually still don't have any capped FUTA years, in part because in the early years, the benefit cost rate is still very high and, in later years, the loans are actually repaid much more quickly here. We'd expect loans to be repaid in 2015 and actually see our point of maximum borrowing in 2012 with only 19% of the loan repayment coming from those FUTA credit reductions. Again, we see the same chart showing where about 3.5% would lie. At 3.5%, that would be higher than the previous peak rate that we've seen in the state, which was 3.22% again in the mid-1970s. This would be slightly higher than those rates but, just for comparison purposes, in general, this is pretty close to where the tax rates were back then.

The final flat rate scenario I have is 4.25% (pg 47). In this, the maximum FUTA reduction is just 0.6%. The FUTA rate in our offset reduction is actually capped at that 0.6% in 2013 so, in 2011 we would expect the FUTA offset to be 0.3%. In the second year, it would be 0.6% and then, in the third year, 2013, it would stay capped at 0.6%.

We’d expect maximum borrowing in this case to occur in 2011 and for loans to be completely repaid in 2014. Here only 9% of that loan repayment would come from FUTA with about $83 million in total interest expense. Because this rate would pay for benefits much sooner and begin repaying the loans much sooner, it really cuts into that interest expense at the cost of a significantly higher tax rate. You can see that would be quite a jump from where we are right now. Beyond about 4 to 4 ½%, I don’t have any tax rate scenarios because one of the features of the unemployment or the way the unemployment taxes work is because we’re on a range from 0.25 to 5.4%. As you start to approach that maximum tax rate of 5.4%, it becomes more difficult to find reserve ratios that spread employers from all, so that they fall into all of those different tax rates. Just for illustration purposes, I generally stop between 4 and 4.5% in all of the scenarios I look at here.

This table shows you (pg 49) all of the different flat rates. You can compare them side-by-side. In general, the higher the tax rate, the lower the interest expense, the higher the cost for SUTA taxes and the lower the cost for FUTA taxes. The total interest from 1.33% would be about $643 million to a flat 4.25% would be about $83 million; interest is essentially the only controllable cost. I hear all of the balance of the Trust Fund loans, as Ms. Jones pointed out earlier, will be repaid either from state unemployment taxes or federal unemployment taxes. Interest is the controllable expense because that’s on top, that’s the extra cost that we have for whatever borrowing takes place. But, balancing the interest repayment against the impact on employers is one of the things the Employment Security Council gets to consider. The next chart (pg 50) just shows all of those different tax rates compared to the historical averages that we’ve seen.

The next sort of general category of repayment strategies I have here is a couple of different ramped rate scenarios. In these scenarios, the average SUTA tax rate is raised by a fixed increment each year. Again, these peak from a 4 to 4.25% and, in contrast to the table we just looked at, here the per employee SUTA cost line represents the additional cost per employee per year. Since tax rates are changing over the course of the years, instead I just showed the amount that would increase each year for illustration.

The first scenario (pg 53) has tax rates increasing by 0.5% each year. I started with a 2% tax rate in each of these three scenarios in 2011 just to have an even number to compare things to for future years so that we didn’t have too many extra decimals in there. It increases then by 0.5% each year capping at 4%, so 2 to 2.5, to 3 to 3.5, to 4. This is the smallest increment that’s presented here and we’d expect loans to be repaid in 2016. In this case, about 19% of the loan repayment would come from FUTA. This is comparable to some of the higher tax rate scenarios because the tax rate eventually gets up to 4% in this scenario. However, in earlier years, while the economy is still kind of weak, the tax rates are a little bit lower at 2% in 2011, 2.5% in 2012. This chart illustrates that. You can see that the tax rate in future years moves up more slowly instead of jumping up to a given rate, because that’s the nature of these ramped scenarios.

The second scenario (pg 55) I present here is three-quarter of a percent steps from 2 to 2.75 to 3.5 and then capping at 4.25%. In this case, we would expect to see the maximum FUTA offset take place in 2015, with FUTA caps being achieved in both 2014 and 2015. We still see loans being repaid in 2016 here and about 14% of the loan repayment coming from FUTA.

Here we see a sharper increase, 0.75% from where we are right now would be about the most comparable to a steady increase in all of the years, because it would be about a 0.67% increase from 2010 to 2011 to go up to that 2% level.

The third (pg 56) and final strategy I have here is a 1% steps to go from where we are now, 1.33 to 2% and then from 2 to 3 and then from 3 to 4. Again, we have capped FUTA years in 2014 and 2015, maximum offset in 2015, loans being repaid in 2016. A lot of these scenarios ended up getting kind of clustered together in part, because the nature of increasing the tax rate by a fixed amount each year, because these are all kind of close together, you see that they all end up kind of crossing the line at about the same time (pg 57).

This table (pg 58) compares the three. You can see the interest expense for the 0.5% total would be about $240 million. For the 1% steps, it would be about $193 million, this is largely due to lower a level of taxes in the earlier years, leading to a higher level of borrowing overall. It keeps it all pretty close together. And, you can see that from starting at 2% in 2011, over the course of two or three years, these tax rates move pretty close together and so they call cross that benefit cost rate line and begin repaying loans at about the same time.

This is the final set of strategies I have here. This sort of answers the question: what if we want to try to cap that FUTA tax rate? We want to take advantage of the ability to cap those increases and make sure that the federal unemployment tax isn't moving up significantly. There are four categories that you have to, or four criteria, that we have to meet, as I mentioned earlier, to achieve those benefit cost rate caps. The two that are sort of in focus here are, that the most that we have to have a tax rate that's at least equal to the five-year average benefit cost rate and we have to have declining loan balances compared to three years ago, in the years that we're trying to achieve the cap. It's also significant that the cap cannot be lower than 0.6%, so we can't try to rush out and cap it at 0.3%, the lowest possible cap is 0.6.

Similar to the ramped rate scenarios, the SUTA costs here are presented as additional costs per employee per year. It's also important to note that, in these scenarios, if you're trying for a cap, once tax rates peak, you can't try to go up and then follow the benefit cost rate down because the state cannot decrease its state unemployment tax effort as one of the four criteria for achieving those FUTA caps. So, once it hits a point, it has to stay there until loans are repaid.

The first scenario (pg 61) is, what if we wanted to cap the FUTA offsets at the minimum possible rate, which is 0.6%. To achieve this, it would require increasing the tax rate by about 1.5% each year for two years and then leaving it capped at about 4.5%. It requires significant rate increases because the challenge that we run into here is that, borrowing would need to be less than in the third prior year. So, if we're looking at 2013, which is the year that this would be in place, we would need borrowing in that year to be less than it is in 2010. Essentially, over the course of the intervening years, the tax rate would have to go up enough to repay all of the loans that take place between now and then, and that requires a significant tax increase. This would achieve a FUTA reduction cap of 0.6%. It would still repay the loans in about 2016 and total interest expenses would be about $120 million. This demonstrates what that tax rate looks like compared to what we've seen before. Maximum borrowing takes place in 2012 because we're trying to get that borrowing to go down by the time we hit 2013.

The second scenario (pg 63) and final one that I present here is to cap the offsets at 0.9% and this would be capping the offsets the year before that BCR add on and that significant jump in the FUTA credit reduction takes place the following year. By capping at 0.9%, smaller tax rates are necessary because we have an additional year to bring in some additional revenue. This could be achieved by increasing the tax rate by 0.7% over four years and then leaving the rate constant, so you would go from 1.33 to 2.2 to 2.7, then to 3.4, and then actually just to 4.0. Here, the target that we have to achieve is that the tax rate has to be at least equal to the benefit cost rate which, if you will remember from several slides earlier in the presentation, in 2013 we expect to be about 3.9%, so the tax rate has to go up to be greater than or equal to that level. I used 4% just for a little extra buffer in these numbers.

In this case, we'd expect about 14% of the total borrowing repayment to come from FUTA. We would be looking at an additional per employee FUTA cost at that cap of about $63. The additional SUTA cost per employee per year would go up by about $186 at the average tax rate and total FUTA offsets would be about $190 million dollars in this scenario. Loans are still repaid in 2016 because the tax rates, by the end of these two scenarios, both end up at nearly the same level. This shows that tax rate on the same chart we've seen several times before.

To compare the two, if we aim for a FUTA cap of 0.6% or 0.9%, this shows us hitting those caps in each year (pgs 65 & 66). The additional SUTA cost per employee per year, in the 0.6% scenario is about $400 compared to about $186 in the 0.9% cap scenario, and the total interest expense is $118 million in the 0.6 scenario and about $217 million in the 0.9% scenario. This shows those two tax scenarios charted out on the graph.

Finally, some final thoughts. There are a lot of numbers in here that say: "when will the loans be repaid", that's a line that appears on all of these tables and I just wanted to make it clear that the point at which the loans are repaid is the point where we have a Trust Fund balance of just zero dollars. That's not regaining solvency for future recessions, that's just the point when the hole has been filled back in. At the Employment Security Council meeting in October, we can present a few less scenarios, but in a little bit more depth, focusing on things like the solvency multiples and any other details that the Council would find useful to consider. The forecasts are expected to change between now and October, because new information will become available. We'll get a few more final employment numbers. That concludes my presentation.

At this point in the presentations, Chairman Havas had a question. For example, you have the employers, many employees with a certain level, payment compensation level as far as their compensation base, and the higher salaried employees: and then you also have this sense of having as your perspective, the greatest number of new employees that can be added by virtue of the policy that is established. What is the counter prevailing negative that is directly related; such as overtime and fewer new employees added by virtue of class-cutting by employers in terms of the economic environment. My question is, can you address the general economic environment as it directly relates to the subject?

Mr. Schmidt answered Mr. Havas. We don't have any good numbers that say what the effect on employment is of these taxes. Especially because the tax rate has been very stable for the last twenty years while Nevada's economy has changed substantially over those times.

We could try to compare it to what the effect was in the 1970s, but there’s a lot of additional information out there. Different environment of the times that would significantly alter any real comparisons we could make. Obviously, as tax rates go up, that is an additional burden on employers and would probably have some negative employment impacts, but I can’t think of any directly, in direct ways that we could try to sample what that effect might be or how to measure it.

Chairman Havas asked if there were any questions from the Council members. Mr. Chairman, if I could make a comment at this point. Chairman Havas gave the floor to Ms. Jones.

Ms Jones mentioned that these strategies that we are viewing are more long term strategies. As we know, last year, we, for the short term, decided to leave the average tax rate alone. Please be reminded, whatever strategy is adopted this year, while a long term strategy towards reaching solvency is our goal, it doesn’t preclude us from adopting different strategies in subsequent years or adjusting our methodology as we go forward. Some of those changes in our methodology going forward, could be impacted by mandates, new laws, whatever that the federal government chooses to implement to address this issue, because it truly is a national issue.

There is discussion at the federal level regarding solvency in the states because, as has been presented to you, most states are in trouble in solvency. Forty states are expected to borrow; only three states are still considered solvent even at this point in time, so it is a national issue. It could be that we have some additional mandates down the road by the federal government that would impact our strategy perspective, so just a reminder on that. As David had alluded to, we can present an infinite number of scenarios and, if there’s some input from the Council of additional scenarios that they would like to see presented in October, or if there are certain scenarios that you would like staff to focus on, we would be happy to receive that input, thank you.

Mr. Havas commented: As we are asked to adopt measures that reflect upon the longer term, it is important that we consider what was just stated.

Council member Paul Barton had one question to ask. “I’m reaching back in my memory in history of the unemployment system, there was a surcharge placed by the legislature at one point to repay loans. Is that a possible scenario now or is that something that is precluded by all the new federal rules?”

One of staff spoke up and asked if ye could field that question. Yes, there was at one point a solvency surcharge that was in the Nevada Statute. That was removed in the late ‘80/early ’90s, I think. It is a possibility, but it really is money that goes into the same bucket. If we say we need to collect $100 or if we need to say we need to collect $95 plus $5 for solvency, it’s still the same $100. Two things that would preclude us from implementing a surcharge at this time: 1) we would have to have the statutory authority and 2) our old benefit system, which it has coded into, it’s up to forty years old, wouldn’t even be able to handle such a surcharge and split that out as a separate tax component in our billing structure.

Once we have our new system in place, which we are in the beginning of a complete system rewrite and that'll be completed in about three years, we would have that additional flexibility in a new system. But, those would be the barriers at this time towards that. Though it could be done, it would be difficult, long story short.

There were no other questions. And Chairman Havas went on to invite Donna Clark to present her overview of the unemployment insurance experience rating process.

VII. OVERVIEW OF THE UNEMPLOYMENT INSURANCE EXPERIENCE RATING PROCESS

Donna Clark, Chief of Contributions for Unemployment Insurance, ESD/DETR

Ms. Clark introduced herself to the Council. Before I start my presentation, which was to give an overview of how the experience rating system works, I believe Mr. Whitacre had a question. I had not prepared anything on that, but I have a few statistics that might help. If, I'm rephrasing basically, you were asking, if the economic conditions have had an impact on collections, employers' ability to pay, is that general? The answer is, of course, absolutely. A few stats to show that, in 2005, 96% of our employers were filing their tax reports and paying those timely. That decreased to 93% by 2009.

You have also heard about the decrease in the employer base. The second quarter of 2008 was our peak, in which we had 60,323 employers that were contributing to the fund, active employers in that regard. At the end of the first quarter of 2010, we were down to 57,170, basically, a 5.2% decrease in our active employer base. Receivables, as a percentage of tax due, at the end of 2005 we were sitting at about 1.8%, that has more than doubled to 3.1%. In putting that into some hard numbers, at the end of the first quarter of 2007, we had about $9 million dollars in outstanding receivables for unemployment insurance. That has risen to $15.6 million at the end of the second quarter of this year. We are seeing a lot more employers leave town without filing those final reports as businesses closes, a lot more payment agreements. Employers who want to pay, who are willing to pay, but who can't pay timely when the report is due, but are negotiating a lot of payment agreements with us. So the collection of those receivables is extending out and taking a lot more time. Does that give you a little perspective?

The purpose of my discussion in preparing you for the October meeting is to provide an overview of how the Unemployment Insurance Tax System works and how the annual averaged tax rate and associated revenue projections are developed. The Unemployment Insurance Program, as David Schmidt talked about earlier, is a joint federal/state partnership created by the Social Security Act of 1935. **Exhibit F is the Overview of the Unemployment Insurance experience Rating Process**.

Under this partnership, the Federal Unemployment Tax Act or FUTA imposes a payroll tax on all employers at a rate of 6.2% of each employee's wages up to $7,000. This equates to a federal payroll tax cost of $434 per employee per year. If, however, a state maintains an unemployment insurance system approved by the U. S. Secretary of Labor, employers are allowed to offset 5.4% of the federal unemployment tax, so they actually pay at a rate of eight-tenths of 1%.

This, of course, the 5.4% is that FUTA offset credit that we have been discussing this afternoon. This of course, reduces the federal tax to $56 per employee per year. Employers who fail to pay state unemployment taxes when due, will not receive the full reduction to their federal unemployment tax. Therefore, State Unemployment Insurance Programs are required to perform a certification process with the Internal Revenue Service for all state unemployment tax payments. The eight-tenths of 1% employers pay to the federal government is used to fund a variety of costs. Some of those primary costs are the fact that federal funds are passed back to the states to cover the administrative costs for the state to run their Unemployment Insurance Programs. It also pays the federal share of extended benefit programs.

The federal UI revenues are also used to build a federal loan fund that Dave has been discussing, from which individual states may borrow whenever it lacks funds to pay UI benefits. And, as Dave mentioned, anything that we pay above that eight-tenths of 1% as FUTA taxes are increased, or anything that we are collecting into the Trust Fund, can also be used to pay back those loans, the principal only of those loans.

The State Unemployment or SUTA taxes collected from Nevada employers are deposited into a Trust Fund. This Fund can only be used to pay benefits to unemployed Nevada workers and the revenue cannot be used for any other purpose, except paying back the principal of those loans. The tax is paid entirely by employers. There is no deduction from employees' paychecks. The tax rates will vary, based on the employer's previous experience with unemployment and, under federal law these funds must be deposited with the U. S. Treasury and cannot be invested in any other manner. That fund does earn interest for us.

At the core of the Unemployment Insurance Tax Program is a rating system known as experience rating. To be in conformity with federal law, all states are required to have a method of experience rating approved by the Secretary of Labor. The way the rating system works is as follows: In Nevada, the rate for all new employers is 2.95% of taxable wages. The taxable wage base or taxable limit is an annual figure calculated at each year as 66, 2/3% of the average annual wage paid to Nevada workers. UI taxes are paid on an individual's wages up to the taxable limit.

In 2010, the taxable wage limit is $27,000 per employee and, as Dave indicated earlier, in 2011, the taxable wage limit will be decreasing to $26,600 per employee. Employers pay at the new employer rate of 2.95% for approximately three and a half to four years until they are eligible for experience rating. Once an employer is eligible for experience rating, an employer's rate can change from 0.25% to 5.4% depending on the employer's experience with unemployment. There are eighteen different tax rate classifications.

The annual tax rate schedule adopted through the regulatory process applies only to experience-rated employers. It has no impact on new employers. The standard rate established by the federal law is 5.4%. Rates lower than 5.4% can be assigned only under a state experience rating system approved by the Secretary of Labor. The intent of an experience rating system is to assign individual tax rates based on an employer's potential risk to the Trust Fund. Basically, those employers with high employee turnover and a greater cost to the Fund pay higher rates than those with low employee turnover.

As displayed on the chart on (pg 6), in 2010, employer costs for unemployment insurance ranged from the highest rate, at the highest rate of 5.4%, equalizing the cost or equaling cost of $1,458 per employee to the lowest rate at 0.25%, which equates to a cost of $67.50 per employee. In calendar year 2011, these costs for an employee will decrease slightly, approximately 1.48%, due to the decrease in the annual taxable wage limit, to determine an employer's experience with the unemployment rating system, this system is essentially cost accounting.

Under the reserve ratio system, the Employment Security Division keeps separate records for each employer to calculate their reserve ratio each year. In the formula used to calculate each employer's reserve ratio (pg 7), we add all of the contributions or the UI taxes paid by the employer and subtract the benefits charged to the employer, that's for the entire history of that account. The result is then divided by the employer's average taxable payroll for the last three completed calendar years. This calculation establishes the employer's reserve ratio.

Now, the purpose of using this method is to put large and small employers on equal footing without regard for industry type. For example, if an employer paid $6,000 in contributions, had $2,000 in benefit charges with an average taxable payroll of $40,000, he would have a reserve ratio of positive 10%. The higher the ratio, the lower his tax rate will be. If an employer has received more benefit charges than he has paid in taxes, his reserve ratio will be negative and, consequently, he will have a higher tax rate. The reserve ratio as calculated for each experience rated employer are then applied to an annual tax rate schedule to determine which rate classification will apply for that calendar year.

Let's look at a sample tax rate schedule (pg 8). In setting the annual tax rate schedule, the eighteen different tax rate classifications, as displayed in the third column of this chart, do not change. These rate classes ranging from 0.25% to 5.4% are fixed by Statute. Instead, the law requires the Employment Security Division Administrator to designate the ranges of reserve ratios to be assigned to each tax rate for a calendar year. In this chart, the range of reserve ratios are shown in columns number one and number two. Using the number of employers assigned to each rate classification displayed in column number four, and the projections of the total taxable wages for the next calendar year displayed in column number six, revenue projections and an average tax rate are then calculated.

In this sample chart, estimated revenues for each rate classification appear in column number eight, and the average tax rate of 1.33% is indicated towards the bottom of the chart. The law also requires the increments between reserve ratios must be uniform. In this sample schedule, the range is from positive 5.2 to negative 17.2, with increments of 1.4 between each of the reserve ratios. If an employer's reserve ratio is a positive 5.2 or better, he gets the lowest rate of 0.25%. So, in our previous example where the employer had a positive reserve ratio of 10%, he would get the lowest rate. An employer with a reserve ratio of less than negative 17.2 would get the highest rate of 5.4 and the rest, as you can see, fall somewhere in between.

In this particular chart, approximately 55% of experience rated employers are in the lowest rate classification of 0.25%. In this sample schedule, there are 35,116 employers eligible for experience rating, which would generate an estimated $249.04 million dollars in revenue to the Unemployment Insurance Trust Fund.

To that, we add the estimate for employers not eligible for an experience rating, $64.61 million, for a total revenue of $313.65 million and, again, an average tax rate of 1.33% for the unemployment tax. You'll note on this chart that we have displayed an additional .05% tax for the Career Enhancement Program. This is a separate state training tax set by Statute. This is being provided for informational purposes only and is not included in those total revenue projections.

In this comparison chart (pg 9), we display a sample of four separate tax rate schedules with different ranges of reserve ratios. Each schedule results in different average tax rates that range from 1% to 2.33%, so you can see by how adjusting those range of reserve ratios that apply to each rate classification, the number of employers in each of the tax rates is changed. This adjustment increases or decreases the average tax rate, and the total estimated revenues. In other words, if you want to increase taxes, and to lower taxes, you select a schedule that puts more employers in the lower tax rates. The number of experience rated employers that fall into each rate classification may also be adjusted by changing the increments between the ranges of reserve ratios.

In this comparison chart (pg 10), the starting point of the range of reserve ratios remains constant at negative 17.2. However, the increments between the ranges of ratios has increased from 1.4 to 2.0. As you widen the increments, more employers are moved from the higher and lower rate classes and shift toward the average tax rate. Each increase in the incrementation also increases the average tax rate and the projected revenues. Before setting the annual tax rate schedule for the next calendar year, Nevada unemployment law requires the ESD Administrator to determine the solvency of the Trust Fund as of September 30th. Projections are then developed for the subsequent calendar year. Those projections include the number of active employers, the amount of taxable payroll, the amount of UI benefits that will be paid, and the estimated revenues the Trust Fund will need to meet those benefit payouts and maintain solvency.

Using employers' reserve ratio data, optional schedules are produced with a variety of average tax rates and revenue projections. In addition to Trust Fund solvency, there are other factors that are considered while setting the annual tax rate schedule, David discussed those earlier, and those do include the current economic conditions and the impact of UI taxes on employers. Typically, Trust Fund financing allows a counter-cyclical method with taxes increased during good economic times to build a reserve fund to support the state in bad economic times. However, this year, as we've illustrated, there are additional extraordinary factors that must also be considered.

The historic level of the current recession has not only depleted Nevada's Trust Fund reserves, it has created a Trust Fund deficit estimated to reach $705 million dollars by the end of this calendar year. The number of active employers and taxable payroll has declined. Nevada has the highest unemployment rate in the nation. Benefits must continue to be paid. Loans must be repaid with interest and the solvency must be eventually restored to the Trust Fund. Therefore, in setting the tax rate schedule for the upcoming calendar year, long term obligations and strategies must also be considered. As representatives of Nevada workers, Nevada businesses, and the general public, it is the role of the Employment Security Council to consider all of the factors and recommend a tax rate schedule to the Employment Security Division Administrator.

A schedule that will protect the solvency of the Trust Fund and best serve the citizens of Nevada. Due to the complexity of the current economic conditions, the purpose of today's meeting was to provide information to the public and the Employment Security Council in preparation for the regulation workshop scheduled for October.

On *October 5, 2010*, the Council will meet again to review updated information on the economy and the status of the Trust Fund and to provide a recommended tax schedule for calendar year 2011. From that point, the Employment Security Administrator will complete the regulatory process for adoption of the annual tax rate schedule. The Employment Security Division will submit the proposed tax schedule regulation to the Legislative Counsel Bureau.

On *October 25, 2010*, the proposed rate schedule will again be reviewed at a small business workshop. The Employment Security Division will hold a public hearing *December 7, 2010* to hear additional testimony and to adopt the rate schedule for calendar year 2011. The Employment Security Division will then submit the adopted regulation to the Legislative Counsel Bureau for review and approval by the Legislative Commission. The approved regulation must be filed with the Secretary of State by *December 31, 2010* for the tax rate schedule to be effective on ***January 1, 2011***. That concludes my overview of how the system works. Ms. Clark concluded her presentation.

Chairman Havas thanked Ms. Clark and invited comments and questions from the members of the Council as well as from the members of the public.

VIII. PUBLIC COMMENT

Mr. Buzz Harris**:** Buzz Harris with the Associated General Contractors. First of all, I would just like to compliment the presentations. They were very nice presentations and I think we all learned a lot through those. One of the questions I have and it was in one of the earlier presentations that hasn't been brought up is: How is the interest paid and maybe I missed that?

Ms. Cindy Jones: If I may address that, Mr. Chairman. For the record, this is Cindy Jones, Employment Security Division Administrator. I'm glad you asked that question. It was a comment that I meant to make before we concluded today. As Mr. Schmidt and others have commented through the process, the rate setting mechanism that we are discussing here can only be used to pay benefits, or to pay back loans and any funds that we collect through the unemployment insurance. SUTA tax cannot be used to pay interest on Trust Fund loans. So, like other states, we will have to come up with a different payment mechanism in order to collect a separate assessment in order to pay those interest costs.

On top of any fluctuations in the SUTA tax that will be charged against Nevada employers, it will be, how do I say this, we will have to add in the impact of that separate assessment that will have to be charged against Nevada employers in order to pay the interest costs. The Division is proposing a Bill Draft Request to be submitted for the upcoming legislative session, so that we can put in a statutory mechanism in order to assess and collect an interest assessment to Nevada employers as we have no such authority in Statute right now.

Other ways that states can pay back interest is through general funds. As I expect, it's well known in this room and those who may be listening, Nevada's general fund probably doesn't have the funding right now to pay that on Nevada employers' behalf, but it is a policy decision that the legislature can make, in lieu of having a separate assessment to pay back those interest charges. So, as we discuss this whole rate setting mechanism and the interest costs, that's a contributing factor to how quickly or how slowly we want to raise the SUTA tax rates, because of the impact on the interest that will have to be paid by Nevada employers.

Chairman Havas: In that context, I would like to add that there should be consideration for what the feds might do in terms of additional suspension of the charging of interest. Cindy, could you respond to that.

Ms. Cindy Jones: Yes. Thank you, Mr. Chair. Right now, as I think Mr. Schmidt had presented, we, like all states, as a result of the stimulus package, are not being charged interest through this current calendar year. It's being deemed paid at the federal level and we will start accruing interest starting January 1^{st} with our first interest payment due September 30^{th} of 2011, is that correct, Mr. Schmidt? Yes. So, we will have to collect, assess, collect, and pay those funds by that time, in order to avoid the decertification process that Mr. Schmidt talked about earlier.

Now, there has been talk at the federal level intermittently about extending the interest-free period and, you know, I can hope. I can lobby for it as much as I can with our federal partners and all interested parties and I expect some states may be in the same situation. The Chairman of our national association or the President of our national association, did testify this year advocating for that on behalf of the states. While not all states were in agreement on that, there were a large number of states that are interested in the federal government providing an extension to the interest-free period, but there's no pending legislation at this time and I'm not sure when we could expect something to be addressed on that issue, I can only hope.

Mr. Buzz Harris: Great. I think that's very helpful. I think as the Council and members of the public and employers that are paying on these taxes and going through these challenging economic times, I think that's one of the things that has to be considered. But, as it sounds like, we're kind of at the mercy, I guess, as far as setting the rate or changing the rate or whatever it may be in October and on into the end of the year, we're kind of at the mercy of what the federal government may do as far as dealing with interest, as well as what the assessment or how things may be drafted through the legislature, which complicates the situation even more.

But, as somebody that represents an association, that works with an association that as we've all heard about how devastated the construction industry is and when it will come back and if it'll come back at what level, I think we all need to really look at different ways of maybe going through a slow process of, maybe the step of moving things up or looking at a very conservative way of going about this so that the impact on the employers, so that people have more of an ability to get back to work is certainly considered. And, you know, I guess, you know, we asked ourselves that question and probably all parts of business is what is the cost of doing nothing and I think that's going to be an issue that's going to come up throughout the legislature and how long are we in this.

I think the presentations today were very informative and I think, you know, as we go through this, we would appreciate the opportunity for public comments and, if you guys have questions about particular industries, we can try and help out as much as possible, thank you.

Chairman Havas: Thank you, Buzz, very much, that was excellent.

Mr. Ray Bacon: For the record, Ray Bacon, Nevada Manufacturers Association. As I told Buzz earlier, it's wonderful that their numbers are so terrible that, even though the manufacturing sector's in second place, nobody pays attention to our problems and things like that, because they make us look like we're light weights.

As I think everybody in this Council realizes, there are no good answers, there are no easy answers and, so consequently, I think what we can do, as the trade associations are, we can bring forward ideas, many of which will involve legislation, many of which will involve very tough decisions. But, I think there are some things that we can do to lessen the impact. The numbers that I calculate out at this stage of the game is we're chewing up money at an average rate of about $55 million a month and our income comes into the neighborhood of about $25 million a month, so we've got a $30 million a month gap that we have to address, plus or minus a little bit, and it also depends on whether the numbers are going up or going down and whether things are getting better or not.

And, if you listen to yesterday's stock report, everything was wonderful and, if you listen to today's report, it pretty much sucks again. So, you tell me what the numbers are going to be in three months and you're probably ready for a Nobel Prize. There are some things, though, that I think that probably can be addressed and at least should be looked at as to whether you want to do anything with it or not.

It adds a level of volatility to the calculation that Ms. Clark talked about, but perhaps you have the ability or, legislatively we could go in and take a look at that three-year rolling average and maybe say we're willing to address that issue and change that to a two-year rolling average. That will mean that employers' rates will rise and fall a little bit faster, but it is still, that still then tends to shift the burden towards those that are causing the problem. As I think everybody in this room realizes, our biggest problem at this stage of the game is the stranded liability of the companies that are going out of business and gone.

I've helped people put the locks on the doors for about sixty firms in the last eighteen months just in my sector alone. And, I know I don't have them all, because every time I send out a dues invoice, I get some that come back as, you know, this company's gone or I get the phone call that says, you know, we're not going to pay this year because we're going to put the lock on the door in the next thirty days or the next sixty days or whatever the magic number is.

There are things that I think you need to address, painful as they will be, and I'm going to hate it at the time, but it still needs to be probably addressed. We probably need to go to the legislature and say that the rate structure that we currently have with the 5.4 to 2.25 range probably needs to change.

Now, whether you change the cap on that and change the 5.4 up, and go up to a higher number there and leave the 0.25 at the bottom or whether you change both ends and/or change the increment, probably all those things need to be on the table and probably you need to go set Bill Anderson and his economists and things like that drive them nuts with various scenarios as far as what happens if you do that. That's probably fair game, but by the time you get back here in October, you probably should be able to see what happens when you do those various scenarios, recognizing that somewhere along the line there's still a $30 million a month that's going to have to be recognized at some point in time.

One of the things that I asked Cindy, because I remembered it was not fixed for years and years on the Worker's Comp thing, and she assured that we did fix it a couple of sessions ago which, quite frankly, right now, is a really good thing, is we used to have for a long time a scenario where a company could go out of business and reconstitute under a new cover name, but still the same principals and things like that and avoid their experience factor. You closed the loop on that in 2007. Right now, that's a really good thing that you did and it went through so fast that I didn't remember whether it had passed or not.

The thing which was not discussed, but I think you need to address at some point in time, is at least a guideline or a long term goal on rebuilding the State Trust Fund. I think, when you get to October, I don't think there's a screaming rush on this thing, but if you take a look at every graph that you saw today, we're six to eight years coming out of this thing and we could be into another recession by the time that thing happens. So, we're probably going to have to address rebuilding the State Trust Fund or we'll come out of this recession just in time to go back into federal borrowing and I don't think any of us want to do that, because we don't like when the feds play the rules.

I can make my wonderful political statement and said if we had anybody in Washington that had any real stroke, they would solve this problem, but that would probably be something that we all know and it's not going to happen. I would recommend that this Council should seriously consider making a recommendation to the legislature that, because we have a lack of economic diversity in this state and that's not going to change, everybody out there, every politician in the world can say everything they want to about green energy and how that's going to bring economic diversity to this state, if you had a one-on-one conversation with the governor, he says he believes that that's going to happen and it's going to be just like gaming. It's going to take us forty years to do that. That means, we're not going to have economic diversity in this state any time soon.

I believe, we should make a conscious decision that our Trust Fund should have a higher limit on it than it's had in the past. I think there is, as we are seeing in this recession, there is a very good reason when you have a narrow, economic base to build that Trust Fund up to another level. It's amazing how far we got. Thank you, Stan Jones, because he was the driver on, as many in this Council know, he was driver on saying: "Nah, keep it there" for years and years and years. But, I don't think we really recognized in this state how narrow our economic base is. We've given all kinds of kudos and things like that for everything we're going to do for economic diversity.

I'm still less than 4% of employment in this state and, if you take a look at the vast majority of the economics in this state are still driven by, primarily by the tourism and gaming sectors, and that is a direct driver for the housing sector and the construction sector. And so consequently, we really have, whether we like it or not, we have an economy that is fundamentally gaming and tourism-based and, because of that, I think there is a strong justification to have a goal that said we're going to stake that State Trust Fund instead of being what the calculation says that we have to have; we can say: "No, we're going to be 25% higher than that number" or maybe 30% or 40% or whatever that number is, but I think there is a reasonable justification for having a long term goal to drive that Trust Fund up.

My contacts back in Washington, which include the National Association of Manufacturers, have had multiple discussions on the whole interest of, the issue of the interest rate and whether there's going to be an extension of the interest rate forgiveness. The answer that I am routinely getting back is not the answer that you want. The answer that I got back was very bluntly: "We're borrowing that money from the Chinese. How far do you want to get in debt to the Chinese?" So, I think I would say, from the comments that I have gotten back from three or four different sources, the odds of an interest rate extension or interest rate forgiveness extension, is slim and that's not the answer we want to hear.

But, when you put it in that perspective of, you know, "We're borrowing the money from the Chinese. How far in debt to the Chinese do you want to go?" and we start counting the votes, right now, with the pressure on not necessarily deficit reduction, but keeping the deficit growth from getting any worse, I think that's probably a realistic appraisal as to where we're at. And, let me look at my full page of notes because I have. Everything I know is on one green card to see if I missed anything, and I don't see anything on here that I missed of significance and things like that. I think this is not going to be fun. This is not going to be pretty. I don't care whether you do a stepped program or whether you do a single rate increase, or you do some combination thereof, we're going to have to do something.

I think the last thing we want to do in this state, by the nature of this state, in the forty–five years that I've lived here, is let the feds control our destiny. We don't like doing that real well. We don't like the fact that they own 87% of the land. We don't like the fact that we have counties that, like Lincoln County with 98.2% federal ownership and, so consequently, they don't have much control over anything in that county and, for us to get the state further to the point where the feds control our destiny, I don't think is something which is in our general nature, even though I think everybody here knows it's going to be painful and nobody's going to enjoy it. With that, I'll take any questions.

Chairman Havas: Thank you, Ray Bacon. You've provided some real leadership in our state. We appreciate it, thank you.

Ms Cindy Jones: If I might make a comment or two, Mr. Bacon. What the Council will be saddled with in October is what the existing law is for setting the rate structure. And, perspectively, if there are some changes to the bottom or the top or the new employer rate or some of those things, those would be perspective years down the road.

So, it will be interesting to see if there are any changes proposed to our rate setting mechanism in Nevada for the upcoming biennium. It is an interest at the federal level, you were talking about some sort of minimum solvency, both in the state and the federal rules right now, Nevada uses a different solvency measure than the federal government does. It's a little shorter term in looking at recessions versus longer terms, so a little more unfluctuating, but there's no minimum solvency level. It says: "Here's what solvency is", there's no requirement within our law that we maintain a Trust Fund at that level. The federal government may be providing incentives to states down the road to have some sort of minimum solvency rules, that's just sort of the rumblings I'm hearing from the other side of the country.

There was one other point that I meant to make and it alludes me for a second. We'll let the Council ask any questions and maybe it'll come back to me. I can't read my own writing, Ray. Oh, I remember what it was. In some of the scenarios that we present for the Council meeting, the scenarios that were presented thus far show how we get to zero, okay? The tax increases ones that we've seen that are just real preliminaries, we said the numbers would change or how to get to zero. I think it would be useful to the Council to say: "And, here's some that show us not only how to get to zero, but to get to what would be deemed a solvent Trust Fund by the next recession" because that's a whole different picture. Digging out of a billion dollar hole is one thing, building up a billion dollar reserve for the next recession paints a whole different picture.

I expect everyone would agree that, you know, to me that says times two, to me, from everything that we've looked at and I think that that would be useful to present to the Council when we go forward. But, the purpose of today's meeting was, of course, to just lay the foundation to help everybody understand the concepts so that, when some of these more robust, in-depth scenarios are presented at the Employment Security Council meeting, at least we have some educational foundation to evaluate those scenarios on, and I certainly appreciate your input and your support over the years.

Mr. Ray Bacon: Part of the reason that I bring up the change in the rate structure and things like that, I recognize that those are statutory changes that you can't make this October.

Ms. Cindy Jones: Right.

Mr. Ray Bacon: But, I think that this Council can come out of your meeting in October with a strong recommendation to the legislature that, we can't really solve this thing long-term with our existing rate structure and with our existing things and, quite frankly, you can tell the legislature: "We need your help. We suggest" you can even come forward with suggested, rough in, changes to the incremented changes to the cap or whatever type scenario and I think it would be the responsible action for, because none of them are going to like the scenario. You will not be popular when you come forward with a recommendation, because they want to move taxes in another direction, but I think it is a firm responsibility of this Council to come forward with the recommendations that says: "Here's what we think you're going to need to do long-term to get us out of this thing". Because I think everybody here knows and agrees that we're in the ditch for the next five, six, seven, eight, nine, ten years. And, so consequently, I don't believe that our existing structure, increment, etc. is going to carry us through that period of time, because we're not going to get everything paid back and get to a viable Trust Fund any time soon.

We all know that, so I think it is clearly incumbent upon this Council to give them some guidelines, to give them some, you know, we need the increment to adjust from a 1.4 to, whatever it is, a 2.0 or something like that and we need the top rate instead of being a 5.4 to be in the neighborhood of a 7 or an 8, so that they've got some sort of rough handle on what we're looking at. You know they're not coming to the party rapidly on the magnitude and the length of the recession. We didn't get there last year rapidly, but I think reality is slowly but surely sinking in and your numbers reflect it probably more than anybody else's numbers that are out there.

Because I work on companies that would like to leave California and Mr. Holt was here earlier that would like to leave California, that would like to leave Oregon, because of things that they've done to move to Nevada. The problem is they can't get financing to move and, so consequently, we'd like to see another fifty or sixty employers every month show up and start businesses here and start employing and start solving our problems. We're not going to get there.

One thing which I didn't include on my card, but let me just mention it because I think it is a worthwhile scenario. Three months ago in a cab in Las Vegas, a guy who was a local native Nevadan, born and raised in, wasn't born in the state, his parents moved him here when he was two, roughly forty-five, this comment that he made to me was that he said what we have done, he said probably 100 to 110 of the 120 employees in the company that he'd been working for, which is now gone completely, were high school drop-outs. And what employers around the entire country are doing is, they are now saying on their applications, from an employer's standpoint, to reduce the size of their applicant pool, because they don't want 1,000 applicants, they are now saying: "high school diploma required" and because of our failures of our K-12 system that we all are well aware of over the last twenty or thirty or forty years, we have a huge percentage of our population that doesn't have a high school diploma. Many of them may have a GED.

If an employer says: "high school diploma required" period, that means that we have some of our folks, whether they came from the gaming industry, the construction industry, or mining industry, they can't move. They are trapped here and his comment was, and I have, it's anecdotal. I couldn't prove it, he couldn't prove it. He said he believes our unemployment rate is a couple of percentage points higher than it should be and could be, because we have people that are trapped here. They can't move because other employers have set the barrier higher than where many of our unemployed people are. It makes sense. It's not profitable, but it scares the hell out of you. Thank you.

Chairman Havas asked if anyone in Las Vegas would like to make a comment or two.

Mr. Art Martinez: Good afternoon, members of the Council. For the record, my name is Art Martinez, Supervising Auditor in the Southern Region. Right now, there appear to be no public comments from Las Vegas. Thank you.

At this point Chairman Havas gave the floor to Cindy Jones.

Ms. Cindy Jones: Mr. Chairman, if there's any information that the Council is interested in asking us to provide for the upcoming meeting; Mr. Bacon, you had made a comment that I believe that Mr. Schmidt may be able to produce some data on and it's the demographics related to education for those that are collecting unemployment insurance benefits. That might be something that we have in our system. I believe we collect some data on that even though it's self-reported let's say, on the education levels for those who file unemployment insurance benefits. It has not gone out and validated, but it might be something that we might be able to present some information on. I'm not sure if it would impact the decision, but it's information that might be out there. And, is there any other information or anything that the Council would like our brilliant staff to focus on for the next meeting?

Chairman Havas said the Council did not have any additional comments. Council member Ross Whitacre wanted to say something.

Mr. Ross Whitacre: I just want to thank the DETR staff for the hard work that they put in to preparing this and to echo Buzz's statements. I think they provided us with a lot of really good information that will go a long ways to helping us make our decisions, appreciate the input from Mr. Bacon also. And, anyway, my comment was a thank you to everybody for their hard work to get ready for this presentation today. It's informative and it's definitely appreciated.

Again it was mentioned that the Employment Security Council Meeting and Regulation Workshop will be held on October 5, 2010 at 10:00 am in this very same room, and also in Las Vegas. It will be broadcast over the Internet also.

IX. ADJOUNMENT

Chairman Havas asked if there was a motion for adjournment. A motion was made and it was seconded. Council signified by saying Aye and the motion carried for Adjournment.

NOTE: These minutes have approved at the Employment Security Council meeting on October 5, 2010.