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Obama Won't Press States to Repay Unemployment Debt

By [SHERYL STOLBERG](#)

President Obama is proposing to come to the rescue of states that face a crushing debt burden after borrowing billions from the federal government to pay unemployment benefits during the recession.

In the 2012 budget he is scheduled to unveil next week, Mr. Obama will defer collecting interest payments on the debt, so states can avoid raising taxes on employers to pay for jobless benefits, according to a person familiar with the plan, who spoke on condition of anonymity because it is not yet final.

With states already cutting services, laying off employees, and raising taxes, this debt burden has been looming as yet another crisis in state capitals around the country. Beginning this fall, the federal government is due to begin charging states as much as \$1.3 billion in interest on the \$42 billion they have borrowed from Washington to help unemployed people weather the recession.

Mr. Obama's plan, which would require the approval of Congress, could run into opposition from Republicans who ran for office vowing to cut government spending and therefore might resist any effort that would reduce federal revenues. But those same lawmakers could also face pressure from Republican governors, who like their Democratic counterparts are scrambling to figure out a way to pay Washington when the federal bill collectors start knocking at the door.

The unemployment benefit system is a joint state-federal venture. The federal government requires states to tax employers on at least the first \$7,000 of an individual's earnings; that money goes into state trust funds to pay the benefits. The federal government also taxes the first \$7,000 of earnings; that money goes into a

federal trust fund.

But with millions of unemployed Americans receiving benefits over the past two years, many state trust funds have run dry, and so states like Michigan, California and New York have turned to Washington for help.

Currently, according to the person who described the administration's plan, 30 states have borrowed a total of \$42 billion from the federal government to pay their share of benefits.

The debt has triggered automatic tax increases for employers in a number of states. Three states – Michigan, Indiana and South Carolina – have already seen their rates rise, and another 20 states are scheduled to see tax rates go up over the next year.

Under Mr. Obama's proposal, the administration would impose a moratorium in 2011 and 2012 on both the state tax increases and the interest payments on the debt.

Then, in 2014, to bring that money back into the federal coffers, the administration proposes to raise the minimum level on which employers pay taxes from \$7,000 of earnings to \$15,000, giving the states the cash they need to cover their debt to Washington.

The administration is betting that the proposal might appeal to Republicans because it involves a tax moratorium. According to the person familiar with it, the White House has calculated that if the plan is adopted, only two states would still owe money to the federal government after a decade. But if the plan is not adopted, this person said, 17 states would still be in debt to Washington.

When they borrowed the money, states hoped that the economy would have turned around by the time the first interest payments came due. But in recent months, in the absence of any offer of help from the federal government, many have been scrambling to figure out ways to pay the money back.

California, which owes \$362 million in interest on a total debt of \$9.7 billion, the highest in the nation, plans to juggle its accounts, borrowing from a trust fund for disabled workers to pay interest to the federal government.

In New York, which owes \$115 million in interest on \$3.2 billion, the cost will be passed on to employers in the form of a tax surcharge. Texas went to the bond market and borrowed \$2 billion to pay back all the money it borrowed from the federal government, judging that the interest on the bonds, which are backed by a tax on employers, would cost less.

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