
SERVICE BULLETIN

Comments About Federal Unemployment Tax (“FUTA”)

May 21, 2010

On May 6, 2010 the U.S. Government Accountability Office released a report to Congress on unemployment insurance trust funds. The GAO report addresses the insolvency of these funds and possible options to improve their financial condition. The combined balance in all state UI trust funds, net of federal loans, is now a negative number (-\$15.4 billion as of the end of 2009) and the Department of Labor projects that net UI reserves will remain negative for several years.

The insolvency of the UI trust funds has put upward pressure on UI tax rates for 2010 and the foreseeable future. The GAO report sums up the problem nicely. For the last three decades UI benefits have remained largely unchanged relative to wages, but employer tax rates have declined relative to wages. This calls into question the collective wisdom exhibited at the state level. Clearly there has been inadequate forward funding, and the state UI trust funds were ill-prepared for the recent recession. The implication of the report is that greater federal involvement or restrictions may be desirable.

The report discusses several possible courses of action for Congress. At the top of the list is the possibility of increasing the FUTA taxable wage base, which has remained at \$7,000 since 1983, and indexing the FUTA wage base to wages. This could induce many states to raise and index their own taxable wage bases. By statute, a state UI wage base may be no less than the FUTA wage base.

Even with no legislation, FUTA taxes can be expected to increase in the next couple of years. For 2009, only Michigan employers incurred a FUTA tax increase of 0.30%, because of the outstanding loan to the Michigan UI trust fund. For 2010, Indiana and South Carolina employers can expect a 0.30% FUTA increase, assuming their loans are not repaid by November 10, 2010. Michigan employers can expect another incremental increase of 0.30% on top of the first increase, so the FUTA tax rate for Michigan employers is destined to be 1.40% (0.80% normal rate plus 0.60% credit reduction). For 2011, twenty-five states may be subject to FUTA tax increases.

A scenario could develop over the next couple of years in which the FUTA wage base is increased and indexed, thereby prompting multiple states to increase and index their wage bases, and the FUTA tax rate starts ratcheting up in multiple states because of outstanding loans, such that these factors taken in combination may result in significantly higher SUI and FUTA tax outlays, even for an employer whose state unemployment tax rate is unchanged.

As always, please feel free to contact us if you have any questions or comments.

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