Employers in 19 States At Risk of Even Higher FUTA Tax Increases

States that continue to have outstanding federal UI loans are at risk of triggering a seldom effective additional Federal Unemployment Tax Increase (on top of the increases that normally trigger at about $21 per employee).

The add-on is called the Benefit Cost Ratio (BCR) add-on. A set of slides explaining the BCR and related FUTA offset credit penalty and relief provisions is attached for reference. There is a waiver of the add-on provided by regulation at http://www.gpo.gov/fdsys/pkg/CFR-2012-title20-vol3/pdf/CFR-2012-title20-vol3-sec606-25.pdf . The waiver must be requested prior to July 1st of the year for which the waiver is requested, and even with the waiver there is still a potential for a lesser increase above the normal $21 per employee increase if the state average tax rate on taxable wages is less than 2.7%.

The additional tax potentially kicks in for a taxable year beginning with the fifth of any succeeding consecutive January 1st that there is a balance due on the loan.

The additional tax varies based on a complicated calculation that compares the average benefits that have been paid to the tax effort in the state. If the tax effort has not met the standard an additional FUTA tax increase, the BCR add-on (additional offset credit reduction) is imposed.

For example, to determine whether the BCR add-on is applicable in 2014, the benefits would be summed from 2008 through 2012 and divided by 5. That result would be divided by taxable wages for 2013 to obtain the BCR. From the greater of that BCR and 2.7 percent, the average tax rate on taxable wages for 2013 would be subtracted and that result is the BCR add-on. (If the result is negative, there is no add-on.)

As you can see from the slides, relief is available in the form of a CAP, avoidance, and a waiver. To obtain a waiver, a state must take no action that will reduce solvency and become effective during the 12 month period ending September 30 in the year for which the waiver is requested. If that is the case, then the 2.7 add-on is substituted and for most states, that add-on will be zero. Even if a state gets the waiver for 2014, the basic 0.3 percent reduction will increment. In 2015, if the state has an outstanding balance on January 1, 2015 and does not have a zero balance at the beginning of November 10, 2015, the BCR add-on would apply for 2015, unless of course the state again applied for a waiver and was successful.

NOTE: Every state calculation is different and requires a careful review of the benefits paid, taxable wages and the average tax rate on taxable wages. Employers and states should review the numbers to make sure that there are no surprises in additional FUTA taxes as a result.

We understand that Indiana and South Carolina are currently reviewing their numbers in anticipation of requesting a waiver of the BCR for 2013.

UWC – STRATEGIC SERVICES ON UNEMPLOYMENT & WORKERS' COMPENSATION
910 17th Street, N.W., Suite 315, Washington, D.C. 20006
Phone (202) 223-8902 • Fax (202) 783-1616 • www.UWCstrategy.org

States first at risk for 2013

Indiana
South Carolina

States first at risk for 2014

Arkansas
California
Connecticut
Florida
Georgia
Kentucky
Missouri
Nevada
New Jersey
New York
North Carolina
Ohio
Rhode Island
Wisconsin

States first at risk for 2015 (if continuing to have outstanding debt)

Arizona
Delaware
Vermont

FUTA Credit Reductions

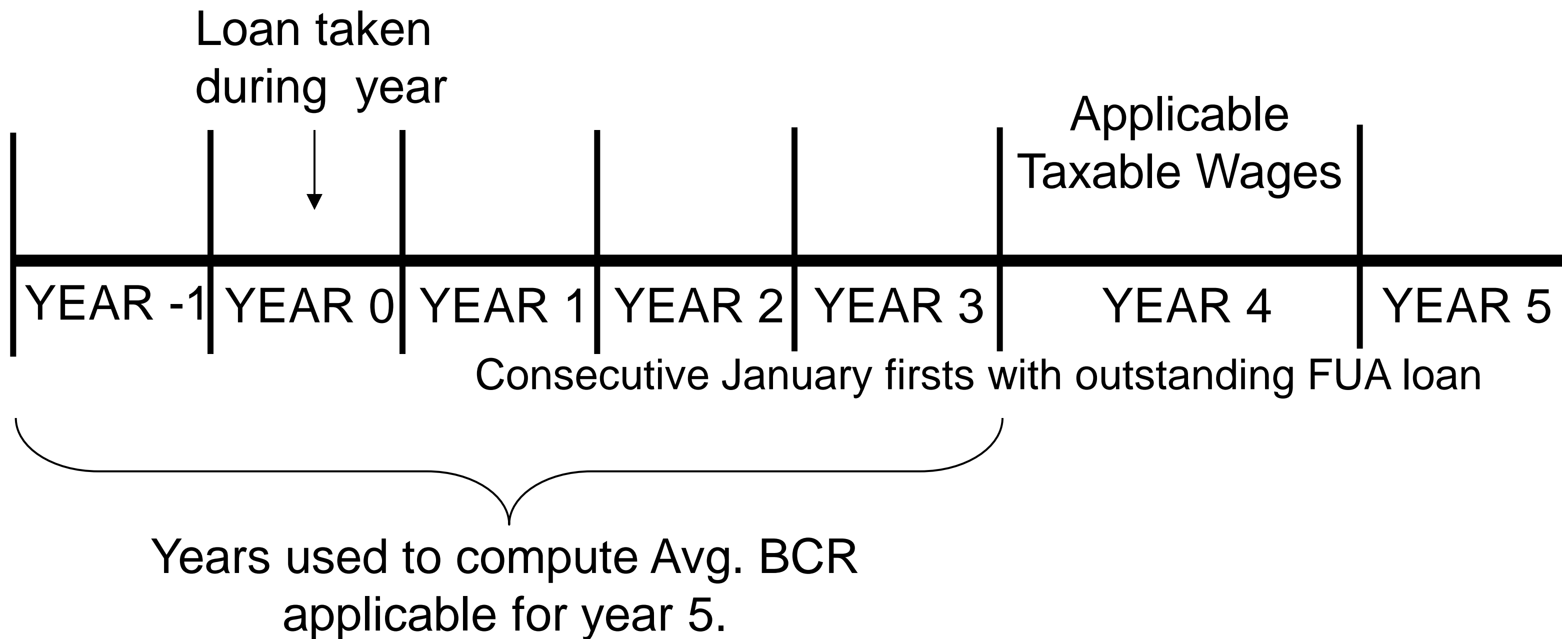
Year	Basic Reduction	Additional Reduction	FUTA Rate
1	0.0%	0.0%	0.6%
2	0.3	0.0	0.9
3	0.6	2.7 Add-on	1.2 or more
4	0.9	2.7 Add-on	1.5 or more
5	1.2	BCR Add-on	1.8 or more
.	.	.	.
.	.	.	.
19	5.4	BCR Add-on	6.0

2.7 Add-on = [(2.7% X 7000/US AAW)-ST ATR_tot] X (ST AAW/7000)

BCR Add-on = (higher of: BCR_tax and 2.7%) – ATR_tax

where AAW = estimated average annual wage (current year)
ATR_tot=average tax rate on total wages (prior year)
ATR_tax = average tax rate on taxable wages (prior year)
BCR_tax = 5-year average benefit cost (ending second prior year) as a percent of taxable wages (prior year)

Benefit Cost Rate



BCR_5 = Avg. Benefit Cost Rate = 1/5 * (sum of benefits year -1 through year 3) / (taxable wages year 4)

Reduced Credit Relief

- AVOIDANCE
  - Allows states to avoid a credit reduction for a given year.
- CAP
  - Caps the credit reduction at the higher of 0.6 percent or the credit reduction applied to the previous year.
- FIFTH-YEAR WAIVER
  - Allows states drop the BCR add-on required in the fifth year and instead use the 2.7 add-on which tends to be smaller.

Avoidance

- To avoid a credit reduction for a taxable year, a State must:
  - Submit an application to the Secretary of Labor prior to July 1 of the year for which avoidance is sought. (See 20 CFR 606.24)
  - Pay the amount that the credit reduction would produce prior to November 10.
  - Repay all FUA loans received during the one-year period ending November 9 prior to November 10.

Avoidance Continued

- Increase solvency for the taxable year through legislative action by an amount equal to or greater than the amount of the FUTA credit reduction.
- Not borrow before the next January 31.

Process

- UI actuaries review application and determine if conditions are met.
- The year on the consecutive January firsts schedule increments.
- See 20 CFR 606.23.

CAP

- To qualify for a cap on credit reductions, beginning with the second taxable year credit reductions are applicable, a state must:
  - Submit an application to the Secretary of Labor prior to July 1 of the year for which a cap is sought.
  - Take no action (legislative, judicial, or administrative) during the 12-month period ending September 30 of the year for which a cap is requested that would reduce taxes or solvency for the period ending September 30.

CAP Continued

- Have an average tax rate on total wages for the taxable year that equals or exceeds the average benefit cost rate for the five years ending with the preceding calendar year.
- The loan balance on September 30 of the taxable year is less than the loan balance on September 30 of the third preceding year.

- **Process**
  - UI actuaries review application and determine if conditions are met.

CAP Continued

- A cap is set at the greater of 0.6 percent or the prior year's level.
- The number of consecutive January firsts with outstanding loans on the credit reduction schedule is not incremented.
- See 20 CFR 606.20 and 606.21.

FIFTH-YEAR WAIVER

- State must submit an application to the Secretary of Labor prior to July 1 of the year for which the waiver is requested.
- Benefit Cost Rate add-on is waived and the 2.7 add-on, which tends to be smaller, applies instead (see 20 CFR 606.25).
- Criterion: Take no action (legislative, judicial, or administrative) during the 12-month period ending September 30 of the year for which the waiver is requested that would reduce solvency for the period ending September 30.
- UI actuaries review application and determine if condition is met.