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LEGISLATIVE UPDATE

Eye on Washington

UNPRECEDENTED FUTA TAX INCREASES MAY APPLY IN 2014

The Federal Unemployment Tax Act (FUTA) tax rate is normally 0.6% of wages paid up to a limit of $7,000 per worker, or $42 per employee per year. However, employers in as many as 13 states and the U.S. Virgin Islands may pay an increased FUTA tax rate in January 2015, based on FUTA taxable wages paid in the affected jurisdictions during 2014.

As background, for-profit employers pay federal and state unemployment insurance (UI) taxes on wages paid. The FUTA tax rate is nominally 6.0%, but includes a credit of 5.4% for payment of state UI taxes, making the effective FUTA tax rate 0.6 %. However, when state UI funds are depleted, states draw from a designated federal loan account, and if such loans are not repaid within two years, part of the 5.4% FUTA tax credit is reduced, thereby increasing the effective FUTA tax rate in affected states.

When this "credit reduction" applies, the FUTA tax typically increases by 0.3%, or $21 per employee, payable in January of the following calendar year with Internal Revenue Service (IRS) Form 940. This credit is further reduced annually by 0.3% until loans are repaid.

In addition, because many of the jurisdictions affected will have had outstanding FUTA debt for five years, they may be subject to a special "Benefit Cost Ratio (BCR)" add-on tax in 2014, which could increase the FUTA tax by more than the typical 0.3% per year. The BCR add-on is less predictable but more substantial; for example, California's effective FUTA rate is expected to increase from 1.5% to 1.8% due to credit reduction alone in 2014. If deemed to be in effect, the BCR add-on tax would add another 1.5%, for a total of 3.3%. The combination of credit reduction and BCR could result in a five-fold increase over the normal FUTA tax rate.

Example:

ABC Corporation pays wages of $50,000 to the corporation's sole employee for 2014. ABC Corporation's FUTA tax due on the individual's wages paid in 2014 would normally be $42 ($7,000 x 0.6%). If the employee worked in California, a credit reduction state, and if the BCR add-on tax is deemed to apply, the total FUTA tax would be $231. For additional information, view this **article** *from the IRS.*

The U.S. Department of Labor (DOL) has identified the states that could be subject to the FUTA BCR add-on and/or credit reduction for 2014. These include:

State	2013 FUTA Rate	2014 FUTA Rate	2014 Estimated BCR Add-on	Total 2014 Potential FUTA Rate	FUTA Tax Per Employee	Increase Over Normal
Arkansas	1.5%	1.8%	0.5%	2.3%	$161	283%
California	1.5%	1.8%	1.5%	3.3%	$231	450%
Connecticut	1.5%	1.8%	0.5%	2.3%	$161	283%
Delaware	1.2%	1.5%		1.5%	$105	150%
Georgia	1.5%	1.8%	0.6%	2.4%	$168	300%
Indiana	1.8%	2.1%	1.2%	3.3%	$231	450%
Kentucky	1.5%	1.8%	1.0%	2.8%	$196	367%
Missouri	1.5%	1.8%	0.4%	2.2%	$154	267%
New York	1.5%	1.8%	0.7%	2.5%	$175	317%
North Carolina	1.5%	1.8%	0.5%	2.3%	$161	283%
Ohio	1.5%	1.8%	1.4%	3.2%	$224	433%
Rhode Island	1.5%	1.8%	1.0%	2.8%	$196	367%
South Carolina	0.6%	2.1%	0.5%	2.6%	$182	333%
Virgin Islands	1.8%	1.8%	1.6%	3.4%	$238	467%

Source: U.S. Department of Labor, June 18, 2014

Employers in the credit reduction states should plan on increased FUTA taxes in 2014 (payable in January 2015). However, states can apply for waivers or pay off FUTA loans during the year to avoid these additional taxes, and many states are announcing such actions. The U.S. DOL will track waiver requests and loan repayments, and determine in mid-November whether additional FUTA taxes will apply to specific states for 2014.

If ADP is responsible for filing Form 940 for your organization, ADP will automatically calculate and pay any additional FUTA tax due as a result of FUTA credit reductions, and you will receive an invoice in January 2015 for credit reduction amounts due with your 2014 IRS Form 940.

ADP Compliance Resources

ADP maintains a staff of dedicated professionals who carefully monitor federal and state legislative and regulatory measures affecting employment-related human resource, payroll, tax and benefits administration, and help ensure that ADP systems are updated as relevant laws evolve. For the latest on how federal and state tax law changes may impact your business, visit the ADP *Eye on Washington* Web page located at **www.adp.com/regulatorynews**.

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