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Unemployment Compensation: The Fundamentals of the Federal Unemployment Tax (FUTA)

Julie M. Whittaker
Specialist in Income Security

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Summary

The Federal Unemployment Tax Act (FUTA) of 1939 specifies the financing arrangement for the Unemployment Compensation (UC) program. Revenue for the program is provided through payroll taxes levied by both the federal government and the states on a portion of wages paid by covered employers. Total UC expenditures include benefit payments and administrative costs.

Federal unemployment taxes are deposited with the U.S. Treasury and credited to the federal accounts within the Unemployment Trust Fund (UTF). Federal unemployment taxes pay for state administrative costs, half the cost of Extended Benefits (EB), and loans to insolvent state UC programs. State unemployment taxes are deposited into the UTF and credited to the corresponding state account. State unemployment tax revenue is limited to paying each state's regular UC benefits and the state's half of EB costs. In budgetary terms, UC benefits are mandatory spending because the underlying law authorizes the Treasury to transfer funds to the states for UC benefit payments without the need for further appropriation.

FUTA imposes a *gross* federal payroll tax on employers of 6.0% on the first $7,000 paid annually to each employee. As an incentive to comply with the framework, FUTA lowers the *net* federal unemployment tax to 0.6% if the state UC program follows the federal requirements. States must follow FUTA guidelines on what types of employment must be covered by UC; and state unemployment taxes on employers must meet FUTA's parameters. All states comply with these guidelines. Because most employees earn more than the $7,000 taxable wage ceiling in a year, the federal unemployment tax paid by an employer is typically no more than $42 per worker per year.

Federal unemployment tax revenue for FY2016 is projected to be $5.8 billion, whereas state unemployment tax revenue is projected to be $40.9 billion. The federal unemployment tax financed expenditures are projected to be approximately $4.2 billion—approximately 12% of all UC expenditures. In comparison, state financed UC expenditures are projected to be $32.3 billion—approximately 88% of all UC expenditures.

There remains significant state independence within the broad parameters set by FUTA. States generally determine individual qualification requirements, disqualification provisions, eligibility, weekly benefit amounts, potential weeks of benefits, and the state tax structure used to finance all of the regular state UC benefits and half of the EB.

Since 1940, Congress has increased the FUTA wage base three times: from $3,000 to $4,200 in 1972; from $4,200 to $6,000 in 1978; and from $6,000 to $7,000 in 1983. Congress has permanently increased the net FUTA tax rate three times: from 0.3% to 0.4% in 1965, 0.5% in 1970, and 0.6% in 1983. There also have been three temporary (surtax) tax rate increases of short duration (from 0.4% to 0.8% in 1962, from 0.4% to 0.65%; in 1963, and from 0.5% to 0.58% in 1973). In addition to these short-term changes, a temporary 0.2% surtax began in 1977 and was continually reauthorized (nine times) until finally lapsing at the end of June 2011—a span of over 34 years.

The combination of increases in the wage base and the doubling of the tax rate has not kept pace with inflation or wage growth, and the proportion of total revenue to total covered wages continues to decline. By 2015, the net federal unemployment tax revenue was equivalent to an *effective tax rate* of 0.1% on the total wages in covered employment.

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Background

The Unemployment Compensation (UC) program is constructed as a joint federal-state partnership providing temporary and partial wage replacement to involuntarily unemployed workers.[1] Federal law sets broad guidelines regarding UC benefits and financing. States administer UC benefits with U.S. Department of Labor (DOL) oversight. State laws establish the program's specifics, resulting in 53 different UC programs operating in the states, the District of Columbia, Puerto Rico, and the Virgin Islands.

UC Administration and Benefits

Titles III, IX, and XII of the Social Security Act (P.L. 74-271, as amended) establish the framework of the UC program. Title III of the SSA authorizes grants to states for the administration of state UC laws, Title IX authorizes the various components of the federal Unemployment Trust Fund (UTF), and Title XII authorizes advances or loans to insolvent states.

UC Financing

The financing arrangement for UC is specified within the Federal Unemployment Tax Act (FUTA)[2] of 1939. Revenue for the program is provided through payroll taxes levied by both the federal government and the states on a portion of wages paid by covered employers. Total UC expenditures include benefit payments and administrative costs. During periods of economic expansion or stability, states fund approximately 90% of all UC expenditures—as almost all of the benefits are state financed by state unemployment taxes. By comparison, federal expenditures are relatively small during these expansions (approximately 10%), in which federal expenditures are primarily administrative grants to the states and are financed by federal unemployment taxes.

Federal unemployment taxes are deposited with the U.S. Treasury and credited to the federal accounts within the UTF.[3] Federal unemployment taxes pay for state administrative costs, half the cost of Extended Benefits (EB),[4] and loans to insolvent state UC programs.[5] (Federal agencies transfer funds into the UTF to pay for benefits for former employees and are not paid by federal unemployment taxes.) Likewise, state unemployment taxes are deposited into the UTF and credited to the corresponding state account. The funds within state UTF accounts are limited to paying each state's regular UC benefits and the state's half of EB costs.

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[1] For a basic description of the Unemployment Compensation (UC) program, see CRS In Focus IF10336, *The Fundamentals of Unemployment Compensation*.

[2] §§3301-3311 of the Internal Revenue Code of 1986 (IRC; 26 U.S.C. §§3301-3311).

[3] For details on the Unemployment Trust Fund (UTF), see CRS Report RS22077, *Unemployment Compensation (UC) and the Unemployment Trust Fund (UTF): Funding UC Benefits*.

[4] UC benefits may be extended at the state level by the permanent law Extended Benefit (EB) program if high unemployment exists within the state. After regular unemployment benefits are exhausted, the EB program may provide up to an additional 13 or 20 weeks of benefits, depending on worker eligibility, state law, and economic conditions in the state. The EB program is funded 50% by federal unemployment taxes and 50% by state unemployment taxes. The EB program was established by the Federal-State Extended Unemployment Compensation Act of 1970 (EUCA; P.L. 91-373) (26 U.S.C. §3304, note). For more details on the EB program, see CRS Report RL33362, *Unemployment Insurance: Programs and Benefits*.

[5] Details on how states may need to borrow funds from the UTF to pay for benefits in CRS Report RS22954, The Unemployment Trust Fund (UTF): State Insolvency and Federal Loans to States (out-of-print report; available from the author).

Recent Trends in Federal Unemployment Tax Revenues and Expenditures

During periods of economic growth, the federal role in financing UC is small relative to the overall size of UC revenues and expenditures. Federal unemployment taxes are dedicated to pay for UC administration grants to the states and the federal share of the EB program, and to fund a federal account within the UTF for state loans. As shown in **Table 1**, federal unemployment tax revenue for FY2016 is projected to be $5.8 billion of the $46.7 billion in all unemployment taxes collected (approximately 12%). Likewise, the projected $5.0 billion in federal spending on administration ($4.2 billion), EB ($0), and benefits for former federal employees (UCFE) and former servicemembers (UCX) ($0.8 billion combined) is much smaller than the projected state spending on regular UC benefits ($32.3 billion).

When economic recessions occur, the UC program is designed to stabilize the economy as federal unemployment expenditures increase through the EB program and additional administrative grants. In addition, the federal government often has augmented the regular UC benefit with temporary unemployment benefit expansions.[6] Thus, at the height of the recent recession, federal expenditures accounted for 60% of the $156 billion paid in total benefits (about $93 billion).[7]

[6] The most recent intervention included the Emergency Unemployment Compensation of 2008 (EUC08; P.L. 110-252). For details on these interventions, see CRS Report RL34340, *Extending Unemployment Compensation Benefits During Recessions*.

[7] As amended, the American Recovery and Reinvestment Act of 2009 (ARRA; P.L. 111-5) contained several provisions affecting EB. Among these provisions was a temporary change increasing the federal share to 100% in the cost-sharing agreement for EB from February 22, 2009, through December 31, 2013. (The permanent funding arrangement is 50% federal funding and 50% state funding.) ARRA also provided federal additional compensation (FAC, a $25 weekly benefit) from February 22, 2009, through June 5, 2010, for recipients of unemployment benefits, including EB. Finally, ARRA also allowed states, at their option, to temporarily change the eligibility requirements for the EB program to expand the number of persons eligible for EB. For details, see CRS Report R40368, *Unemployment Insurance Provisions in the American Recovery and Reinvestment Act of 2009*.

Table 1. Revenue and Expenditures Associated with Unemployment Compensation, FY2005-FY2016

(dollars in billions)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
UC Revenue, Total	**41.8**	**43.0**	**41.0**	**39.4**	**37.8**	**44.7**	**55.9**	**64.8**	**54.5**	**52.4**	**51.9**	**46.7**
Federal Unemployment Tax	6.7	7.1	7.3	7.2	6.7	6.4	6.6	5.4	5.5	5.5	5.8	5.8
State Unemployment Taxes	35.1	35.9	33.7	32.2	31.1	38.3	49.3	59.4	49.0	46.9	42.2	40.9
UC Outlays, Total	**32.0**	**31.02**	**32.12**	**42.42**	**119.6**	**156.1**	**116.6**	**90.2**	**66.2**	**41.6**	**32.5**	**33.1**
Regular Benefits (UC)	31.2	30.2	31.4	38.1	75.3	63.0	48.5	44.3	39.6	35.9	31.7	32.3
Extended Benefits (EB)[a]	0.0	0.02	0.02	0.02	4.1	8.0	11.9	4.9	0.1	0.0	0.0	0.0
Emergency Unemployment Compensation [b]	—	—	—	3.6	32.7	72.1	52.7	39.6	25.4	4.8	—	—
Federal Additional Compensation[c]	—	—	—	—	6.5	11.7	1.9	—	—	—	—	—
UCFE/UCX[d]	0.8	0.8	0.7	0.7	1.0	1.3	1.6	1.4	1.1	0.9	0.8	0.8
Administrative Costs	**3.8**	**3.9**	**3.7**	**3.9**	**4.3**	**5.5**	**5.0**	**4.9**	**4.8**	**4.4**	**4.0**	**4.2**

Source: U.S. Department of Labor (DOL), *UI Outlook*, January 2001-January 2016, and *UI Outlook Midsession Review FY2017,* July 2016 and updates.

Notes: Projected for FY2016.

a. The federal share of EB increased to 100% from February 22, 2009, through December 31, 2013. (The permanent funding arrangement is 50% federal funding and 50% state funding.)

b. A temporary unemployment insurance program, the Emergency Unemployment Compensation (EUC08) program, began in July 2008 and ended in December 2013. For details on EUC08, see CRS Report R42444, *Emergency Unemployment Compensation (EUC08): Status of Benefits Prior to Expiration*.

c. The Federal Additional Compensation (FAC) was a temporary, federally funded, $25 weekly additional benefit for individuals who were receiving regular UC, EB, EUC08, Trade Adjustment Assistance (TAA), and Disaster Unemployment Assistance (DUA) benefits. The FAC was first authorized from February 17, 2009, until June 2, 2010.

d. UC benefits for civilian federal employees (UCFE) and former military servicemembers (UCX) are paid by the former employing agency.

Unemployment Taxes and the Budget

All unemployment tax revenue and expenditures for benefits and administration flow through the U.S. Treasury, and thus affect federal revenue, outlays, and the overall financial position (deficit or surplus) of the federal government. However, as a practical matter, all UC and EB financial transactions occur within the trust fund.

Both federal and state unemployment tax revenue as well as administrative and benefit expenditures within the UTF are accounted for in the federal budget.[8] Federal unemployment taxes are deposited into the UTF. The Treasury invests all receipts in federal securities that bear interest. Similarly, state unemployment taxes are credited to each state's account within the UTF, and the Treasury invests all receipts in federal securities that bear interest. The investment of state unemployment revenue in federal securities increases the federal debt. When states pay UC benefits to unemployed individuals, the Treasury redeems those securities held within that state's UTF account. Thus, the payment of regular state UC benefits decreases the federal debt.

UC Benefits Are Mandatory Entitlements

In budgetary terms, UC benefits are mandatory spending because the underlying law authorizes the Treasury to transfer funds to the states for UC benefit payments without the need for further appropriation.[9] In other words, UC benefits are not subject to the annual appropriations process.[10] Because UC benefits are mandatory entitlements, even if a state's trust fund account is depleted, the state remains legally required to continue paying benefits. To do so, the state might borrow money either from the dedicated loan account within the UTF or outside sources.[11]

Appropriations for UC Administration

Each fiscal year, Congress appropriates funds through the federal budget process to pay for both the federal and states' costs of administering unemployment compensation programs. The Secretary of Labor determines (*certifies*) the amount of the administrative payments and permits the Secretary of the Treasury to make the payments to the states.[12]

[8] For basic information on the budget process, see CRS Report 98-721, *Introduction to the Federal Budget Process*.

[9] 42 U.S.C. 1104(f).

[10] Federal spending is divided into two broad categories: discretionary spending and mandatory spending. Mandatory spending is composed of expenditures controlled by laws other than appropriations, including federal spending on entitlement programs. See CRS Report RL33074, *Mandatory Spending Since 1962*, for trends in mandatory spending. Discretionary spending is provided and controlled through appropriations acts, which fund many of the activities commonly associated with such federal government functions as running executive branch agencies, congressional offices and agencies, and international operations of the government.

[11] Details on the mechanics of the loan process in CRS Report RS22954, The Unemployment Trust Fund (UTF): State Insolvency and Federal Loans to States (out-of-print report; available from the author).

[12] The U.S. Department of Labor (DOL) determines administrative grants using the Resource Justification Model (RJM). The RJM is designed to reflect the states' current methods of administering the UC program, including their adoption of new technologies. The RJM collects data from state cost accounting records and allows states to justify additional resources above the levels in the cost accounting data for the budget year. Current state allotments are available at http://ows.doleta.gov/unemploy/budget.asp.

Calculating the Federal Unemployment Tax

FUTA imposes a 6.0% *gross* federal unemployment tax rate on the first $7,000 of each worker's yearly earnings. However, FUTA provides tax incentives to states, which may lower the net tax rate, if states meet federal UC program guidelines.

Net FUTA Rate: 0.6%

Employers in states with UC programs approved by the U.S. Labor Secretary and with no outstanding federal loans[13] may credit up to 5.4 percentage points of state unemployment taxes paid against the 6.0% tax rate, making the minimum net federal unemployment tax rate 0.6%.[14]

This tax credit is provided by two separate Internal Revenue Code (IRC) provisions.

1. Section 3304 of the IRC provides for a *state tax credit* for all employers of up to 5.4%.
2. Section 3303 of the IRC provides an *additional tax credit* for state employers if the employer paid less than 5.4% in state taxes if the state unemployment tax schedule is such that employers generating the fewest claimants have the lowest tax rates (e.g., *experience rates* its employers).[15]

The total of the state tax credits (state plus additional) cannot exceed 5.4%. Conventionally, these two tax credits are generally aggregated and discussed as the 5.4% state tax credit. This report follows this convention.

Taxable Wage Base: $7,000 of Each Worker's Yearly Earnings

The taxable wage base for federal unemployment tax is limited to no more than the first $7,000 of each worker's yearly earnings. Because most employees earn more than the $7,000 taxable wage ceiling in a year, the federal unemployment tax typically is $42 per worker per year. That is, $7,000 × 0.6%, or just over two cents per hour for a full-time, year-round worker.[16]

[13] Employers in states that have outstanding federal UTF loans may have a reduced state tax credit. Details on this potential reduction in CRS Report RS22954, The Unemployment Trust Fund (UTF): State Insolvency and Federal Loans to States (out-of-print report; available from the author).

[14] §3304 of FUTA (26 U.S.C. §3304) allows up to 5.4% credit for *actual* state unemployment taxes paid. In addition, under §3303 of FUTA (26 U.S.C. §3303), employers that paid less than a 5.4% rate in state unemployment taxes are eligible for an *additional* state tax credit of up to 5.4%. The total state tax credit (actual and additional) on federal unemployment tax calculation is restricted to be no more than 5.4%. Thus, all employers in states with approved UC programs receive a 5.4% credit in the calculation of FUTA, even if the employer paid less than a 5.4% rate in state unemployment taxes.

[15] For example, an employer paying a state tax rate of 0.9% would have a state tax credit of 0.9% and would also receive an additional credit of 4.5% (5.4-0.9), resulting in a net FUTA tax of 0.6% on the first $7,000 of earnings per employee. For a detailed discussion of experience rating, see the section "Experience-Rating of Employer Taxes."

[16] The calculation assumes a full-time, year-round worker works 52 weeks per year and 40 hours per week (for 2,080 hours per year), $42 ÷ 2080 hours = $0.0202/hour and that all state tax credit reductions are available to the employer.

Legislative History and Brief Analysis of the Changes in Federal Unemployment Taxes

As to be expected, the federal unemployment tax has changed substantially since 1936. The **Appendix** provides a comprehensive list of changes in the federal unemployment tax law that altered either the taxable wage base or the tax rate. There have been many other changes within FUTA, including the expansion of covered work and specific uses of tax revenue, which are not explored in this report. DOL provides a chronology of major changes to UC law, accessible at http://workforcesecurity.doleta.gov/unemploy/pdf/chronfedlaws.pdf.

Changes in the Taxable Wage Base

The original Social Security Act of 1935 imposed the federal unemployment tax on total annual wages (and required the states to implement a state unemployment tax on wages as well). The decision to tax total wages "was in keeping with the principle of imposing a tax that would apply uniformly throughout the country so that no state would have an advantage over another."[17] However, in 1939, the Social Security Board recommended that taxes be limited to the first $3,000 of annual wages—the same taxable wage base to which Social Security payroll taxes were applied at the time.[18] Because the $3,000 ceiling exceeded annual wages of 98% of all workers in 1939, it reduced revenues from the unemployment tax only slightly.[19]

Since 1940, Congress has increased the FUTA wage base three times: from $3,000 to $4,200 in 1972; from $4,200 to $6,000 in 1978; and from $6,000 to $7,000 in 1983.[20] These increases did not keep pace with inflation or wage growth, and the divergence between taxable and total wages continues to grow as shown in **Figure 1**. Applying the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) to adjust for inflation, the $7,000 taxable wage base in 2015 is equivalent to $487 in 1940, approximately one-sixth of the actual tax base ($3,000) in 1940.[21]

[17] William Haber and Merrill G. Murray, *Unemployment Insurance in the American Economy* (Richard D. Irwin, Inc., 1966), p. 359. (Hereinafter Haber and Murray.)

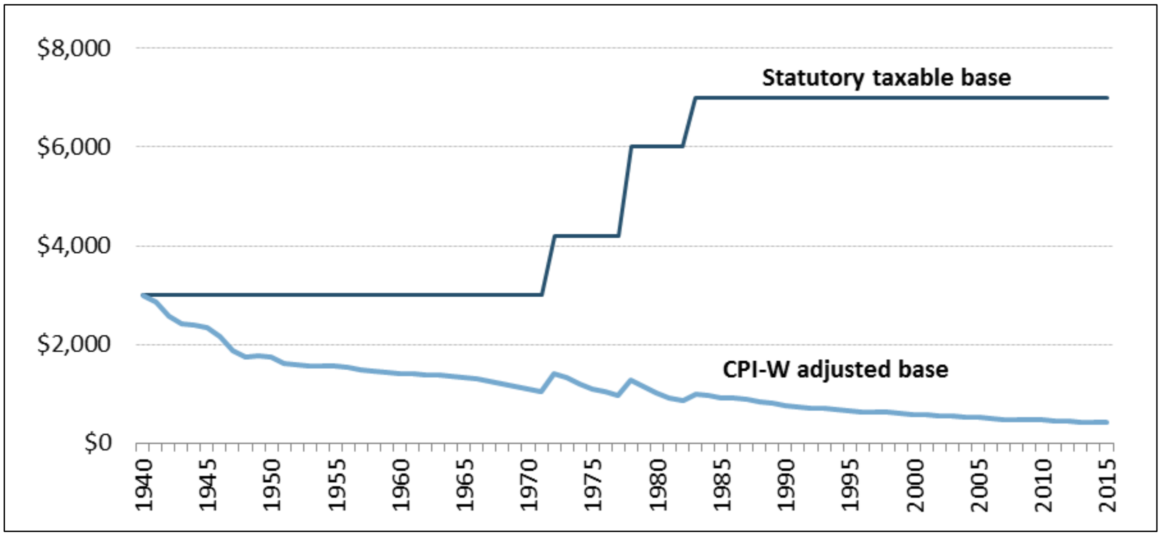
[18] Social Security Board, *Proposed Changes in the Social Security Act*, A Report of the Social Security Board to the President and to the Congress of the United States, Washington, DC, 1939, p. 18, https://www.ssa.gov/history/reports/38ssbadvise.html.

[19] Haber and Murray, Table 18-1, p. 360.

[20] P.L. 91-373, P.L. 94-566, and P.L. 98-248, respectively.

[21] The Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) was used for the inflation adjustment as it was the only index available for use in 1940. Alternatively, a wage base of $49,300 would be required to adjust the original $3,000 ceiling for the effect of inflation from 1940 through 2015.

Figure 1. FUTA Taxable Wage Base (Nominal Dollars) and CPI-W Adjusted Base (1940 Dollars), 1940-2015



Source: Congressional Research Service (CRS).

Notes: Federal Unemployment Tax Act (FUTA) tax base as required under law.
Adjusted base applies the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) to calculate the value of the statutory taxable base in 1940 dollars. The CPI-W was used for the inflation adjustment as it was the only index available for use in 1940. Adjusting the original $3,000 ceiling for the effect of inflation from 1940 through 2015 would result in a wage base of $49,300.
Congress has increased the FUTA wage base three times: from $3,000 to $4,200 in 1972 (P.L. 91-373); from $4,200 to $6,000 in 1978 (P.L. 94-566); and from $6,000 to $7,000 in 1983 (P.L. 98-248).

Changes in the Tax Rate

The original Social Security Act of 1935 provided for a gradual increase in the net tax rate (from 0.1% in 1936, to 0.2% in 1937, to 0.3% in 1938) and was applied to all covered annual wages. Since 1939, Congress has permanently increased the net FUTA tax rate three times: from 0.3% to 0.4% in 1965, 0.5% in 1970, and 0.6% in 1983. These increases partially offset the erosion of the taxable wage base. (See the previous section "Changes in the Taxable Wage Base" for details.)

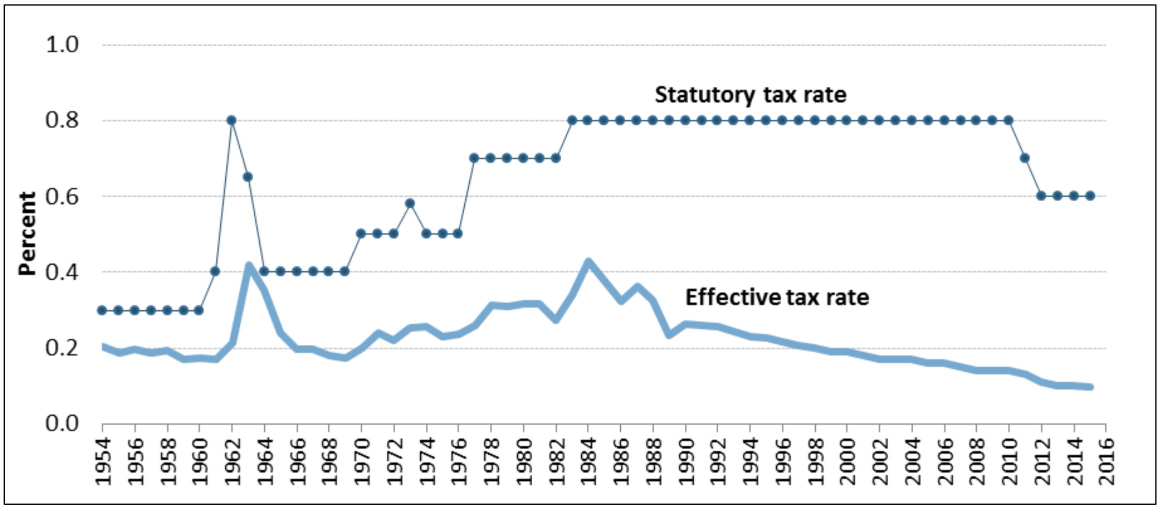
In addition to these three permanent tax increases, there have been three temporary (*surtax*) increases[22] of short duration. In addition to these short-term changes, a temporary 0.2% surtax began in 1977 and was continually reauthorized (nine times) until finally lapsing at the end of June 2011—a span of over 34 years.[23]

[22] In 1962, a temporary 0.4% surtax was authorized, increasing the net tax from 0.4% to 0.8%. In 1963, a temporary 0.25% surtax increased the net tax from 0.4% to 0.65%; in 1973, another temporary surtax increased the net tax from 0.5% to 0.58%.

[23] P.L. 94-566 first imposed the 0.2% surtax, increasing the net FUTA tax from 0.5% to 0.7% on the first $6,000 of earnings. The surtax was to be eliminated when all advances to the states had been repaid. P.L. 97-248 extended the surtax (increasing the net FUTA tax from 0.6% to 0.8%, on the first $7,000 of earnings) until the Emergency Unemployment Compensation Account (EUCA, an account dedicated to funding the EB program) loans were repaid. By 1998, the EUCA loans were about to be repaid, but P.L. 100-203 extended the 0.2% surtax for three years—until January 1991. P.L. 101-508 extended the surtax for five years—until January 1996. P.L. 102-164 extended the surtax for an additional year—until January 1997. P.L. 103-66 extended the surtax for an additional two years—until January 2000. P.L. 105-34 extended the surtax for an additional nine years—until January 2008. P.L. 110-140 and P.L. 110-343 each extended the surtax for one additional year. P.L. 111-92 extended the surtax for 1.5 years from December 2009 (continued...)

Figure 2 depicts the changes of the *net federal unemployment tax rate* since 1954. In addition, it provides information on the *effective tax rate* (i.e., the total federal revenue as a proportion of total wages in covered employment). Although the statutory tax rate has doubled since 1954, the effective tax rate has decreased from 0.2% to 0.1%—the result of limited increases in the taxable wage base.

Figure 2. FUTA Tax Rate and Estimated Effective Tax Rate Controlling for Wage Growth, 1954-2015



Source: CRS figure based upon data provided by U.S. DOL, Employment and Training Administration, Office of Unemployment Insurance.

Note: Effective tax rate is total FUTA revenue as a proportion of total wages in covered employment.

Federal Unemployment Taxes: Payment Timing and Requirements for Employers

Required Quarterly Payment

Once employers owe more than $500 in estimated federal unemployment tax, they are required to pay the federal unemployment taxes on a quarterly basis.[24] Employers must use Internal Revenue Service (IRS) Form 940,[25] an annual tax form, to reconcile the quarterly deposits to the actual tax liability. For most employers, the fourth quarter employment taxes from the previous year are due on January 31. This is also the payment in which any additional taxes attributable to a reduced state tax credit would be due. IRS Instructions for the federal unemployment tax are available at http://www.irs.gov/pub/irs-pdf/i940.pdf.

(...continued)

through June 2011.

[24] Employers that are required to pay FUTA on a quarterly basis use IRS Form 941. Employers also use the form to report withheld income taxes, Social Security tax, or Medicare tax from employee's paychecks and to report the employer's portion of Social Security or Medicare tax. Form 941 is available at https://www.irs.gov/pub/irs-pdf/f941.pdf.

[25] Available at https://www.irs.gov/pub/irs-pdf/f940.pdf.

Annual Payment

If the estimated quarterly federal tax is less than $500, an employer may roll the liability over to the next quarter until either when the liability is $500 or more or when the annual income tax is due. At that point, the employer must pay FUTA taxes to the Treasury.

FUTA: Guidelines for State UC Programs

FUTA provides guidelines from which states construct UC benefits, coverage, and state financing. As an incentive to comply with the framework, FUTA provides a lower net federal unemployment tax if state UC programs meet certain guidelines on what types of employment must be covered by the state UC programs and meet the state unemployment tax requirements set out under FUTA. There remains significant state independence within these broad parameters. States generally determine individual qualification requirements, disqualification provisions, eligibility, weekly benefit amounts, potential weeks of benefits, and the state tax structure used to finance all of the regular state UC benefits and half of the EB.[26]

FUTA: Coverage

For most employers, FUTA requires that all positions be subject to the federal unemployment tax if an employer paid wages of at least $1,500 during any calendar quarter or employed at least one worker for at least one day of each of 20 weeks in the current or prior year. The federal coverage requirements have expensive net tax implications for state employers if they are not met. The 5.4% state tax credit on the federal unemployment tax is not allowed if a job is required to be covered under FUTA, but the state UC program does not cover that job.

States may cover additional types of employment that are not required to be covered by FUTA. However, most states have chosen not to expand unemployment insurance coverage significantly. The following employment generally is not covered by the unemployment insurance system:

- self-employment,
- work done by relatives,
- work of patients in hospitals,
- work by student interns,
- work by alien farmworkers,
- seasonal camp employment, and
- railroad workers (who have a separate unemployment program).[27]

Exceptions

There are exceptions to the broad FUTA coverage requirements. Certain nonprofit organizations; state and local governments; services provided while employed by federally recognized Indian

[26] For details on state UC laws, see U.S. DOL, Employment and Training Administration (ETA), Office of Unemployment Insurance (OUI), *The Comparison of State Unemployment Insurance Laws*, Washington, DC, 2016, http://ows.doleta.gov/unemploy/pdf/uilawcompar/2016/complete.pdf.

[27] For information on railroad UI, see CRS Report RS22350, *Railroad Retirement Board: Retirement, Survivor, Disability, Unemployment, and Sickness Benefits*.

tribes; certain agricultural labor; and certain domestic service all have different thresholds for coverage.

- *Nonprofit employers* are subject to coverage requirements if the organization employs at least four workers for one day in each of 20 different weeks in the current or prior year.
- *State or local governments and Indian tribes* are subject to coverage requirements without regard to the number of employees.
- *Agricultural employers* are subject to coverage requirement if the employer paid cash wages of at least $20,000 for agricultural labor in any calendar quarter or employed 10 or more workers for at least one day in each of 20 different weeks in the current or prior year.
- *Domestic service employers* are subject to the coverage requirement if the employer paid cash wages of $1,000 or more for domestic service during any calendar quarter in the current or prior year.

Contingent on state laws, certain nonprofit, state or local government organizations, and federally recognized Indian tribes may opt to be a *reimbursable employer* in which the employing agency has the option to reimburse the UC program for benefits paid to their laid-off employees rather than pay state and federal unemployment taxes.

FUTA: State UC Tax Requirements

FUTA provides basic guidelines for state unemployment taxes. States may opt to experience rate employers, tax employers that generate the most claimants at a rate of at least 5.4%, and have a taxable wage base of at least the first $7,000 of each employee's annual earnings.

If a state meets these minimum tax requirements, FUTA allows a *state tax credit* of up to 5.4% to be applied against federal unemployment taxes. In addition, if a state *experience rates* its employers (where employers who minimize UC claims have a lower state unemployment tax), FUTA provides an *additional tax credit* for state employers. This credit ensures the employer who paid less than 5.4% in state taxes receives a full 5.4% state tax credit (when combined with the state tax credit).

Experience-Rating of Employer Taxes

Federal law allows states to experience rate their employers within their state unemployment tax schedule. Experience rating requires that states set up their tax systems such that employers generating the fewest claimants have the lowest tax rates. The state unemployment tax rate of an employer is based on the amount of UC paid to its former employees. In general, the more UC benefits paid to its former employees, the higher the tax rate of the employer—up to a cap established by state law. The experience rating is intended to ensure an equitable distribution of UC program taxes among employers and to encourage a stable workforce. All states use experience rating when determining an employer's state unemployment tax rate.

State Tax Rate

Federal law remains silent on the lowest state unemployment tax rate that may be applied to employers. Indeed, federal law only sets a floor of 5.4% on the state's *maximum* unemployment tax rate to be applied to employers with proportionately the highest claims from former workers.[28]

As a result of these few requirements, state unemployment tax rates have wide variation. In tax year 2015, several states (Iowa, Montana, and South Dakota) applied a tax rate of 0% to employers with the fewest claims from former workers. In comparison, the maximum state unemployment tax rates ranged from a lower bound of 5.4% (the lowest allowed under federal law) in Florida, Georgia, Idaho, Nebraska, Nevada, Oregon, and Puerto Rico to the highest ceiling of 11.13% in Massachusetts.

Taxable Base

Federal law requires the taxable wage base on which the state unemployment tax is applied must be at least $7,000 per worker per year.

In January 2016, state ceilings on taxable wages ranged from the $7,000 federal minimum (Arizona, Arkansas, Florida, and Puerto Rico) to $44,000 (Washington State).

[28] For a list of all state tax structures, see U.S. DOL, ETA, OUI, *Significant Provisions of State Unemployment Insurance Laws,* January 2016, http://ows.doleta.gov/unemploy/content/sigpros/2010-2019/January2016.pdf.

Appendix. Laws Impacting Federal Unemployment Taxes, 1935-Present

Table A-1. Federal Changes in Unemployment Taxable Wage Base and Tax Rate

Public Law and Enactment Date	Taxable Wage Base	Tax Rate	State Tax Credit	Net Tax Rate
P.L. 74-271 Title IX of the Social Security Act (SSA) Signed into law on August 14, 1935, Declared constitutional on May 24, 1937	All covered wages	1936: 1.0% 1937: 2.0% 1938: 3.0%	0.9% 1.8% 2.7%	1936: 0.1% 1937: 0.2% 1938: 0.3%
P.L. 76-1 moves the taxing provision in Title IX of the SSA to what is now Chapter 23 of Internal Revenue Code (IRC) February 10, 1939	All covered wages	3.0%	2.7%	0.3%
P.L. 76-379, Social Security Amendments of 1939 Names the taxing provisions of the IRC the "Federal Unemployment Tax Act," August 10, 1939	$3,000 1940	3.0%	2.7%	0.3%
P.L. 86-778, Social Security Amendments of 1960, September 13, 1960	$3,000	1962: 3.1%	2.7%	0.4% 1962
P. L. 87-6 Temporary Extended Unemployment Compensation Act of 1961 (TEUC) 1962 and 1963 March 24, 1961	$3,000	1962: 3.1%+0.4% temporary surtax P.L 87-6 also authorized surtax for 1963 but was overwritten by P.L. 88-31	2.7%	0.8% 1962 (0.8% in 1963; however, overwritten by P.L. 88-31)

Public Law and Enactment Date	Taxable Wage Base	Tax Rate	State Tax Credit	Net Tax Rate
P.L. 88–31 To amend title IX of the Social Security Act with respect to the amount authorized to be made available to the States out of the employment security administration account for certain administrative expenses, to reduce the rate of the Federal unemployment tax for the calendar year 1963, and for other purposes. May 29, 1963	$3,000	1963: 3.1%+0.25% temporary surtax 3% 1964: reverts to 3.1%	2.7%	1963: .65% 1965: reverts to 0.4%
P.L. 91-373 Employment Security Amendments of 1970 August, 10, 1970	1973: $4,200	1970: FUTA 3.2%	2.7%	0.5%
P.L. 92-329 To provide for a six-month extension of the emergency unemployment compensation program June 30, 1972	$4,200	1973 3.1% +0.18% surtax 1974: reverts to 3.1%	2.7%	1973- 0.58% 1974-returned to 0.5%
P.L. 94-566 Unemployment Compensation Amendments of 1976 October 20, 1976	1978: $6,000	1978: 3.2% +0.2% surtax until loans were repaid	2.7%	1977: 0.7% (until loans repaid)
P.L. 97-248 Tax Equity and Fiscal Responsibility Act of 1982 September 3, 1982	1983: $7,000	1983: 3.3%+ 0.2% surtax 1985: 6.0% + 0.2% surtax	1983-1984:2.7% 1985: 5.4%	1983-1984: 0.8% Reverts to 0.6% once loans repaid.
P.L. 100-203 Omnibus Budget Reconciliation Act of 1987 December 22, 1987	$7,000	1988-1990: 6.0% + 0.2% surtax extension	5.4%	1988-1990: 0.8%
P.L. 101-508 Omnibus Budget Reconciliation Act of 1990 January 4, 1991	$7,000	1991-1995: 6.0% + 0.2% surtax extension	5.4%	1991-1995: 0.8%

Public Law and Enactment Date	Taxable Wage Base	Tax Rate	State Tax Credit	Net Tax Rate
P.L. 102-164 Emergency Unemployment Compensation Act of 1991 November 15, 1991	$7,000	1996: 6.0% + 0.2% surtax extension	5.4%	1996: 0.8%
P.L. 103-66 Omnibus Budget Reconciliation Act of 1993 August 10, 1993	$7,000	1997-1998: 6.0% + 0.2% surtax extension	5.4%	1997-1998: 0.8%
P.L. 105-34 Taxpayer Relief Act of 1997 August 5, 1997	$7,000	1999-2007: 6.0% + 0.2% surtax extension	5.4%	1999-2007: 0.8%
P.L. 110-140 Energy Independence and Security Act of 2007 December 19, 2007	$7,000	2008: 6.0% + 0.2% surtax extension	5.4%	2008: 0.8%
P.L. 110-343, Title IV of the Emergency Economic Stabilization Act of 2008, October 3, 2008	$7,000	2009: 6.0% + 0.2% surtax extension	5.4%	2009: 0.8%
P.L. 111-92, Worker, Homeownership, and Business Assistance Act of 2009 November 6, 2009	$7,000	2010-June 2011: 6.0% + 0.2% surtax extension July 1, 2011: reverts to 0.6%	5.4%	2010-June 2011: 0.8% July 1, 2011: reverts to 0.6%

Source: Congressional Research Service.

Author Contact Information

Julie M. Whittaker
Specialist in Income Security
jwhittaker@crs.loc.gov, 7-2587