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# Questions and Answers About FUTA Taxes

By National Employment Law Project

**What is the FUTA tax?** The Federal Unemployment Tax Act (FUTA) imposes a payroll tax on the first $7000 paid to covered employees in a calendar year. The gross 6.2 percent federal tax is reduced by credits for all employers in states with approved state UI laws to an net effective tax rate of .8%. Since all states have approved state UI laws, this .8% tax rate translates to an annual maximum $56 FUTA tax bill for each covered employee paid wages under FUTA.

**What is the FUTA surcharge?** The current net effective FUTA rate of 0.8% has two components. Beginning in 1977, Congress added a 0.2% surcharge to the then existing permanently authorized FUTA tax rate. The 0.2% surcharge is currently authorized through December 31, 2007. The permanently authorized FUTA tax rate is 0.6%.

**What are FUTA revenues used for?** FUTA tax revenues are estimated for FY2001 at $6.9 billion. FUTA taxes pay for the federal administration of UI programs, including state agency operations and USDOL's UI activities, as well as supporting federal trust funds that pay the 50% federal share of extended benefits and provide loans for insolvent state UI trust funds. FUTA revenues are held in legally dedicated trust funds solely for these UI-related uses.

**Why has Congress kept the FUTA surcharge in place?** The FUTA surcharge was extended due largely to federal budget deficit considerations in 1987, 1990, 1993, and 1997. Other UI restrictions passed largely for budgetary reasons as well—including federal income taxation of UI benefits, restrictions on the EB program, and mandated pension offsets—also remain in place for the same reasons. If Congress revisits the FUTA surcharge in light of today's budgetary surpluses, fairness dictates that it should also re-examine these continuing federal restrictions on UI benefits as well.

**What is the history of FUTA tax rates?** Both the amount of wages subject to FUTA taxes (the "taxable wage base") and the net tax rate imposed on taxable wages have been adjusted by Congress from time to time since the enactment of UI in 1935. The taxable wage base was initially set at $3000 in 1939, was raised to $4200 in 1972, and lifted to $6000 in 1978. The current $7000 taxable wage base was set in 1983 and has not been raised since that time. The net effective tax rate has ranged from 0.3% in 1939 and reached 0.7% by 1977. It was raised to 0.8% in 1983. In terms of total payrolls, FUTA tax rates have ranged between 0.2 % to 0.3% over UI program history and currently fall in the low end of this range.

**Are current FUTA taxes too high?** When inflation or growth in wages are taken into consideration, FUTA payroll tax revenues produced by the current net tax rate applied to the low taxable wage base are at or near their the lowest levels over the entire history of the UI program. In 1939, the $3000 taxable wage base subjected over 90 percent of covered wages to FUTA taxation. The $7000 FUTA taxable wage base covers far less wages today. The 0.8% net tax amounts to only 3 cents per hour for full-time workers. There is simply not much factual support for an argument that FUTA taxes are too high.

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