

# Prepare for Payroll Tax Hikes to Replenish Unemployment Insurance Funds

State UI funds were depleted as unemployment rates spiked

By Stephen Miller, CEBS

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In response to the COVID-19 pandemic, state unemployment insurance (UI) benefits, funded through payroll taxes, were exhausted. As a result, the percentage of employees' wages that employers pay for UI programs is expected to at least double over the next two to three years, benefits advisors predict.

"There will be much higher unemployment benefit tax costs in the future, and those should be planned for," said Gage Stille, a principal at HR consultancy Buck in New York City. "Employers will need to respond to these higher anticipated costs."

## Pre-Pandemic Benefits

Before the pandemic, states provided an average maximum weekly benefit of approximately \$450, and most states provide a weekly benefit up to a maximum of 26 weeks, Stille said during a Buck webinar

([https://f.hubspotusercontent10.net/hubfs/4828910/buck\\_ppt\\_unemploymentbenefitcosts\\_4.22.21\\_final.pdf](https://f.hubspotusercontent10.net/hubfs/4828910/buck_ppt_unemploymentbenefitcosts_4.22.21_final.pdf)) in April. When unemployment rates hit a state-defined threshold, "states potentially provide 13 to 20 weeks of extended benefits," he said.

In 2020 and 2021, however, "these coverage levels have evolved rapidly during the pandemic, where we've seen benefit durations extended and also a rise in the total weekly value of benefits."

*[SHRM members-only HR Q&A: What are the new reasons individuals may now collect unemployment under the CARES Act?*

([www.shrm.org/resourcesandtools/tools-and-samples/hr-qa/pages/what-are-the-new-reasons-individuals-may-now-collect-unemployment-under-the-cares-act.aspx](http://www.shrm.org/resourcesandtools/tools-and-samples/hr-qa/pages/what-are-the-new-reasons-individuals-may-now-collect-unemployment-under-the-cares-act.aspx))

Exhausted state UI funds will mean significant cost increases to employers, Joe Kane, executive vice president at Total Management Solutions Inc., a severance management services business, said during Buck's webinar. "There were approximately 82 million new unemployment claims made from March 2020 to March 2021," he noted, far exceeding the job losses during the 2008 recession.

Citing Bureau of Labor Statistics (BLS) figures, Kane said that the unemployment rate increased from 3.5 percent in February 2020 to 14.8 percent in April, and then fell to 6.7 percent in December.

The April 2020 peak represented the highest overall unemployment rate since BLS data collection began in 1948, he said.

Another change: Before the pandemic, "only 4.4 percent of unemployed people collected unemployment benefits for more than the 26-week period that states provide normally. Now, we have over 43 percent of unemployed people collecting greater than 26 weeks."

As Congress created new federal payment programs and offered supplemental payments to the unemployed, many states also extended benefits based on high unemployment rates.

"The surge in initial claims caused a reduction in taxable wages—making the situation [for state UI funds] even worse," Kane said.

While the federal government provided states with billions of dollars to help reimburse some of the costs of extended benefits, "states were not required to allocate funds to their UI trust funds," Kane noted. Instead, the federal government "gave states the latitude to use the funds for other needs as well."

### Reviewing the Basics: SUTA (or SUI) Taxes

State unemployment insurance (SUI) benefits are funded by State Unemployment Tax Act (SUTA) payroll taxes, collected by each state. These taxes are also referred to as SUI taxes. Federal Unemployment Tax Act (FUTA) payroll taxes go into a fund that pays for the federal government's oversight of state unemployment insurance programs.

For the majority of states, SUTA is an employer-only tax.

Employers pay SUTA taxes on their employees' wages, at a percentage rate set by the state (<https://www.patriotsoftware.com/blog/payroll/what-is-my-state-unemployment-tax-rate/>).

In each state, the SUTA tax is applied up to certain wage thresholds. "For some states, it's the first \$7,000 of wages paid, in other states it might be the first \$10,000, and in some states it's over \$40,000," Kane explained.

There are also differing formulas that states use to calculate SUTA tax rates, he noted. "In most states, the more employees you lay off, the higher your 'experience rate' will be, and the higher your SUI taxes will be," Kane said.

### SUI Tax Rate Hikes

Altogether, state funds had more than \$80 billion available prior to the pandemic, Kane said. "That has been completely drawn down," he added. "In many cases, states are significantly overdrawn, and when that happens, many states draw on a federal line of credit."

Collectively, states have borrowed more than \$50 billion from the federal government, Kane said, "and these federal loans have to be repaid along with replenishing state insurance funds to get them back to a healthy funded level."

There's no question, he added, that "increased unemployment taxes are in store for employers."

The "aftershock" of this, Kane said, means the average state UI payroll tax rate of 1.78 percent is expected to double in the next few years "at least for some period of time," unless states enact legislative changes to their UI programs, such as cutting benefits. "There's no question UI tax rates are going to go to 3.5 percent [on average]. I think it's going to go closer to 4 percent before this is done."

Kane advised employers to take actions such as:

- **Discussing expected rate increases** with their UI claims manager.
- **Conducting unemployment fraud exams ([www.shrm.org/resourcesandtools/legal-and-compliance/state-and-local-updates/pages/coronavirus-unemployment-fraud-pandemic.aspx](http://www.shrm.org/resourcesandtools/legal-and-compliance/state-and-local-updates/pages/coronavirus-unemployment-fraud-pandemic.aspx))** to filter out fraudulent claims.
- **Reviewing their tax rate for layoffs** and correcting errors to their rate.

Most states use June 30 as the computation date to determine SUI rates for the upcoming calendar year, Kane noted. "Anticipate some impact in 2021 but expect the real impact to be felt in 2022 and later" as federal loans to the states need to be repaid, he advised.

### Expanded UI Benefits Make Hiring Harder

Many employers say they can't hire because extended, expanded federal and state UI payments have caused potential job candidates to drop out of the labor force. Meanwhile, employers' UI taxes are also going up.

"It does seem like a double hit," Kane said.

He pointed out that the American Rescue Plan Act, for instance, provides an additional 29 weeks of unemployment benefits to people who exhaust their regular state benefits—with \$300 per week supplemental coverage—into September 2021, following earlier federal UI supplemental payments under prior legislation.

"There are circumstances where workers can claim up to 99 weeks of unemployment benefits," Kane said, with \$750 per week in benefits on average, "and higher in some states."

*Business Insider* recently reported that "the reopening of businesses across the U.S. that are looking to hire, along with enhanced unemployment benefits, has cut into the number of applicants (<https://www.businessinsider.com/mcdonalds-pays-50-for-job-interviews-highlighting-hiring-struggles-2021-4>)," according to business owners.

Similarly, the *Dayton Daily News* reported that restaurants are struggling with short staffing, and some owners point to unemployment checks that have been extended (<https://www.daytondailynews.com/local/restaurants-struggle-with-short-staffing-as-more-people-return-to-dining/5ECZEBFJUNAXLMTFSLQB5W4ESQ/>) to September.

*The Wall Street Journal* reported that "supplemental federal unemployment benefits of \$300 a week for laid-off workers this year are a barrier to bringing back employees (<https://www.wsj.com/articles/restaurants-serve-up-signing-bonuses-higher-pay-to-win-back-workers-11619359201>), some restaurant owners and economists said. Federal and average state unemployment payments can surpass the weekly pay of an employee working 40 hours at \$15 an hour."

The *Journal* also reported, "Proponents of the supplemental unemployment benefits have said the measures remain necessary to support out-of-work people still struggling with COVID-19's economic fallout, and give unemployed workers time to search for better-paying jobs."

#### State Push-Back

Montana Gov. Greg Gianforte, a Republican, announced on May 4 that the state will be the first in the nation to end federally subsidized \$300-a-week expanded unemployment benefits in favor of a one-time \$1,200 bonus (<https://montanafreepress.org/2021/05/04/expanded-unemployment-benefits-are-out-return-to-work-bonuses-are-in/>) for Montanans who re-enter the workforce.

"Montana is open for business again, but I hear from too many employers throughout our state who can't find workers," Gianforte said in a statement. "Incentives matter, and the vast expansion of federal unemployment benefits is now doing more harm than good. We need to incentivize Montanans to reenter the workforce."

[SHRM members-only toolkit: *Managing Unemployment Compensation Costs and Caseload* ([www.shrm.org/resourcesandtools/tools-and-samples/toolkits/pages/unemploymentcostsandcaseload.aspx](http://www.shrm.org/resourcesandtools/tools-and-samples/toolkits/pages/unemploymentcostsandcaseload.aspx))]

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