

# FUTA Credit Reduction: Overview and Process

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## What is a FUTA Credit Reduction?

The Federal Unemployment Tax Act (FUTA) provides employers with a federal tax credit when state unemployment taxes are paid on time. If a state has outstanding federal unemployment loan balances for multiple consecutive years, the U.S. Department of Labor (DOL) may reduce this credit.

This reduction increases the effective FUTA tax rate for employers in affected states and is commonly referred to as a FUTA credit reduction.

**\*Note\*** TempWorks refers to the following [DOL website](#) for FUTA Credit Reductions.

- Historical FUTA Credit Reductions include the final rates.
- Potential Credit Reductions are what TempWorks uses for estimated rates.

**\*Note\*** The U.S. Department of Labor (DOL) has published its estimated credit reduction rates for 2026. Based on these estimates, **California** and the **U.S. Virgin Islands** are the jurisdictions forecasted to be affected this year:

- **California:** 5.3% (including a 3.8% BCR Add-On)
- **U.S. Virgin Islands:** 4.8%

As part of our annual process, we use these preliminary estimates to recalculate liabilities back to January 1st, 2026. **These rates will be updated with the 4/3/2026 release, and the associated recalculation amounts will be reflected in the open weekend bill date.** Once the rates are finalized later this year, a second recalculation will be performed to reflect any adjustments.

**Important note for California clients:** The **Benefit Cost Rate (BCR) add-on** remains in effect for 2026. This surcharge is applied on top of the standard credit reduction for states with outstanding federal unemployment loans and can significantly increase FUTA tax liability. Clients with California payroll may see a notable increase in their tax amounts in upcoming reports. For those using our Payroll, Funding, or Tax processing services, these liabilities will be collected on your behalf.

For clients utilizing Payroll, Funding, or Tax processing services, these changes will impact funding and wire reports. For clients not using these services, the changes may affect tax reporting and gross profit.

# How the Process Works

Each year, the DOL evaluates states with outstanding federal unemployment loans to determine whether a FUTA credit reduction applies. Preliminary estimates of potential credit reductions are typically published in February or March, followed by final, official rates in November or early December.

Once these rates are published, both estimated and final, we update our production environment as part of our standard release process. During this update, we perform a recalculation back to January 1 of the current year to ensure all applicable wages and tax amounts reflect the most current information.

These updates are documented in our standard release notes so clients can see when changes have been applied. In cases of larger impacts, such as higher-than-usual rate changes or additional adjustments like a Benefit Cost Rate (BCR) add-on, we provide a separate communication to give clients additional context and visibility into the expected impact.

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## Differences by Customer Type

The impact of FUTA credit reduction updates and how they are managed depends on the services a client uses.

### Payroll, Funding, or Tax Processing Clients

For clients utilizing TempWorks payroll, funding or tax processing services, FUTA credit reduction updates are handled end-to-end within the system. When estimated rates are released, rates are updated and liabilities are recalculated year-to-date based on the estimated rate. Any resulting change in liability is either collected from or returned to you at that time.

Once final rates are published, the same process is applied, with year-to-date liabilities recalculated and any resulting adjustments collected or refunded accordingly. This approach ensures your filings remain accurate and compliant without requiring any action on your part.

**\*Note\*** These updates can have a significant impact on payroll and tax obligations. Changes such as the BCR add-on can affect overall payroll costs and may require additional planning with your customers. Being aware of and preparing for these updates can help you manage cash flow effectively and keep your payroll, tax, and funding processes running smoothly.

### Software-Only Clients

For clients **not** using TempWorks payroll, funding, or tax processing services, we update the FUTA credit reduction rates in the system and perform a recalculation back to January 1 of the year. Clients who leave the rate as published will see corresponding changes reflected in their tax and gross profit reports.

**\*Note\*** Software-only clients also have the option to request that TempWorks Support insert a temporary override on the rate for them. Clients who choose this option should understand that it is their responsibility

to contact us to have the override removed, for example when final rates are published at the end of the year. Overrides are **not automatically removed** on the client's behalf.

Clients should proceed with caution when requesting an override. In certain situations, such as the California BCR, even if a waiver is requested, there is no guarantee it will be approved.

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## Additional Information

- FUTA credit reductions **only apply** to employers in affected states.
- The impact varies based on wages subject to FUTA tax and the applicable reduction rate.
- Estimated amounts are **subject to change** until final rates are published by the DOL.

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