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Private Request for Analysis: Niskanen Center

Budgetary effects of FUTA reform

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Proposal

This report considers proposed reforms to the Federal Unemployment Tax Act (FUTA) wage base, all of which would come into effect in 2026. Currently, FUTA taxes are imposed at a 0.6% rate on the first $7,000 of each employee's annual wages and are implemented as an employer-side payroll tax. This wage base has remained unchanged since 1983, despite wage growth and inflation over the past four decades.

We explore reforms along two dimensions of policy:

- **What is the value of the wage base?** We show results for each $1,000 increment between the current-law value of $7,000 and a doubling to $14,000.
- **Is the wage base indexed?** We show results for three options: no indexing, inflation indexing (chained CPIU), and wage indexing (SSA's average wage index) starting in 2026.

Estimated Budgetary Effects

Table 1 below presents estimated net revenue effects over the ten-year budget window starting in 2026. These estimates account for both the additional FUTA revenue generated and the offsetting reduction in income tax revenue that occurs when employers reduce wages to partially offset higher payroll tax burdens. Appendix Table 1 shows the full year-by-year estimates.

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Table 1. Estimated Ten-Year Budgetary Effects, CY2026-35 (Billions of Dollars)

Wage Base	No Indexing	Inflation Indexing	Wage Indexing
$8,000	6	11	16
$9,000	13	18	23
$10,000	19	25	30
$11,000	25	32	37
$12,000	31	38	45
$13,000	38	45	52
$14,000	44	52	59

Source: The Budget Lab calculations.

There are three important analytical takeaways from this exercise:

- **The income tax offset reduces net revenue raised by about one-quarter.** Because labor markets are competitive (i.e., workers generally earn their marginal revenue product), an increase in one form of labor compensation must be offset by a decrease in other forms. Employer-side payroll taxes like FUTA are a component of the cost of labor; therefore, an increase in FUTA means that other forms of compensation, like taxable wages, must fall, all else equal. This reduction in taxable wages reduces the base for income taxes, creating an "income tax offset" roughly equal to the economy-wide marginal tax rate on wages. We estimate this offset dynamic is about 25% of the additional gross FUTA revenues raised.
- **Wage base increases have slightly nonlinear revenue impacts.** That is, doubling the wage base leads to a slightly less-than-doubling in FUTA revenues. This is because some (part-time) workers make more than $7,000 but less than $14,000.[1]
- **The indexing mechanism affects long-term revenue.** Wage indexing produces the highest revenue estimates, as it keeps the ratio of FUTA revenue to wages paid constant over time (all else equal). Inflation indexing provides more moderate growth in revenues, keeping the real value of FUTA taxes paid constant.

Methodological Assumptions

We estimated the budget effects of this proposal using our tax microsimulation model. Model version 2989c41 is used to generate the numbers in this report. Our baseline estimates are benchmarked to the DOL's historical and projected FUTA receipts for 2021-2023.

[1] We project that baseline FUTA revenues will be about $64B over the decade. If revenues doubled with the wage base, the net revenue estimate for the "no indexation, $14,000" option would be about $64B x (1 – 25%) = $48B. Instead the net revenue estimate is $44B.

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Appendix

Appendix Table 1. Estimated Annual Budgetary Effects (Billions of Dollars)

Indexing and Wage Base Details	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	Budget Window
No Indexing											
$8,000	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.7	0.7	0.7	6.4
$9,000	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	12.8
$10,000	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	19.1
$11,000	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.6	2.6	2.6	25.3
$12,000	3.1	3.1	3.1	3.1	3.1	3.1	3.2	3.2	3.2	3.2	31.5
$13,000	3.7	3.7	3.7	3.7	3.7	3.7	3.8	3.8	3.8	3.8	37.6
$14,000	4.3	4.3	4.3	4.3	4.3	4.4	4.4	4.4	4.4	4.4	43.6
Inflation Indexing											
$8,000	0.6	0.7	0.8	0.9	1.1	1.2	1.3	1.4	1.5	1.7	11.3
$9,000	1.3	1.4	1.5	1.6	1.7	1.9	2.0	2.1	2.3	2.4	18.1
$10,000	1.9	2.0	2.2	2.3	2.4	2.5	2.7	2.8	3.0	3.2	25.0
$11,000	2.5	2.6	2.8	2.9	3.1	3.2	3.4	3.6	3.7	3.9	31.7
$12,000	3.1	3.3	3.4	3.6	3.7	3.9	4.1	4.3	4.4	4.6	38.4
$13,000	3.7	3.9	4.1	4.2	4.4	4.6	4.8	5.0	5.2	5.4	45.0
$14,000	4.3	4.5	4.7	4.8	5.0	5.2	5.4	5.6	5.9	6.1	51.6
Wage Indexing											
$8,000	0.6	0.8	1.0	1.2	1.4	1.6	1.9	2.1	2.3	2.5	15.6
$9,000	1.3	1.5	1.7	1.9	2.2	2.4	2.6	2.9	3.1	3.4	23.0
$10,000	1.9	2.1	2.4	2.6	2.9	3.1	3.4	3.7	4.0	4.3	30.3
$11,000	2.5	2.8	3.1	3.3	3.6	3.9	4.1	4.4	4.8	5.1	37.5
$12,000	3.1	3.4	3.7	4.0	4.3	4.6	4.9	5.2	5.6	5.9	44.6
$13,000	3.7	4.0	4.4	4.6	5.0	5.3	5.6	6.0	6.4	6.8	51.7
$14,000	4.3	4.6	5.0	5.3	5.6	6.0	6.4	6.8	7.2	7.6	58.7

Source: The Budget Lab calculations.