First Nonprofit Group
An AmTrust Financial Company

Nonprofits Employing Exemptions:

How Participation in an Alternative Unemployment Program Satisfies SUI Responsibilities with Minimal Risks and Costs

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Introduction

Nonprofit organizations often rely on lean budgets and revenue from various and sometimes unpredictable sources. Private donations and government funding can change quickly and drastically as a result of issues completely outside of an organization's control. For this reason, most nonprofit organizations must strive to keep costs under control to maintain services when financial tides turn. While nonprofits are exempt from a majority of state and federal taxes, they are not without costly obligations, such as those associated with unemployment insurance claims.

Funding of the Federal Unemployment Tax Act

Since the 1930s, employers have paid Federal Unemployment Tax Act and State unemployment taxes. FUTA taxes are used primarily to pay for the administrative costs associated with unemployment insurance by funding state workforce agencies. The money is also used to build a fund balance, which states can draw from when unemployment rates spike. FUTA also pays one-half of the cost of extended unemployment benefits.

Employers pay FUTA tax at a rate of 6 percent of the taxable wage base, which is offset by credits of up to 5.4 percent. Ideally, this means that employers would pay a FUTA rate of 0.6 percent on the taxable wage base, $7,000, for a total of $42 per employee. However, penalties in the form of credit reductions to employers are levied on states that have outstanding federal UI loan debt. When these loans remain outstanding for more than two years, the federal government lowers the standard tax credit for employers, increasing the effective FUTA tax rate by 0.3 percent each year until the loan is repaid.

Nonprofits are exempt from paying FUTA taxes, but are still responsible for contributing to state unemployment insurance tax pools in order to cover their benefit claims.

The Great Recession delivered a heavy blow to many state UI trust funds that were underfunded and ill-prepared for the sharp increase in unemployment insurance claims. This led to massive borrowing by some states in order to pay UI benefits. The length and scope of the recession has prevented many states from paying back the debt within two years and as 2013 draws to a close, employers in sixteen states could see reductions to their FUTA tax credits.

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State Unemployment Insurance Tax Pools

State unemployment tax is paid directly to state workforce agencies and used solely for the purpose of paying unemployment benefits. Tax rates vary for each employer depending on its experience rating, a calculation based on an employer's history of past payroll in ratio with claims paid for unemployment insurance. Employers have seen SUI tax rates increase as states struggle to pay back federal loan debts. For many states, the mandated FUTA increases alone could take years to whittle down the large debt loads.

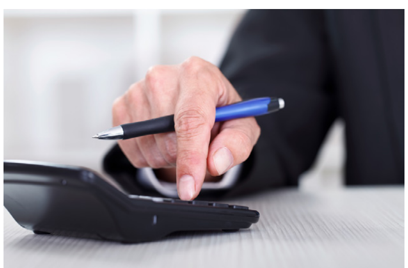
Even though nonprofits effectively avoid the federally mandated increases associated with FUTA tax, they will still experience an increase in UI costs as SUI tax rates increase in states to help pay down their federal loan debt.

Even during stable economic times, employers typically overpay their state unemployment insurance costs. There is no reimbursement for employers that typically pay $1.20 to $2.50 for every dollar spent on UI claim costs. An unemployment claim of $7,000 can cost an employer between $8,400 and $17,500. This is compounded by the fact that state unemployment systems themselves overpay benefits at an average rate of 10.81 percent.

Involvement in SUTF is costly, unpredictable and for nonprofits, unnecessary.

There are also socialized aspects to the systems that fund state unemployment trust funds. In addition to contributions for their own workers, employers are paying to cover the UI claim burden of companies that have gone out of business or experienced claim costs that were higher than their tax contributions. Involvement in SUTF is costly, unpredictable and for nonprofits, unnecessary.

Reimbursement Financing: Nonprofit Options for Satisfying SUI Responsibilities



While nonprofits and government agencies are not exempt from contributions to SUI, they are provided a unique opportunity to opt out of the associated tax pools. Utilizing the reimbursement method, nonprofit organizations reimburse state unemployment compensation funds only for the amount of benefits paid to their former employees. This allows the nonprofits to avoid the costs associated with varying rates, overpayments and the socialized costs built into SUI programs.

If a nonprofit has no turnover resulting in UI claims and operates as a reimbursing employer, then it would have no UI costs for the year.

However, there are risks associated with becoming a reimbursing employer. The option provides no insurance against excessive unemployment claims, creating unprotected liabilities. If a self-insured nonprofit experiences an unexpected increase in unemployment claims it will not have the backing of an SUI trust fund to cover the cost of those claims. The cost of reimbursing the state for large UI claims can place an organization's programs at risk for cutbacks and lead to more unemployment. Organizations may also lack trained staff who understand complex SUI law and in turn wind up over-paying claims.

There are different options for nonprofits that choose the reimbursement method over the taxable one. One option for nonprofits that want to opt out while reducing the risk of self-insuring is to join a group trust. While group trusts provide nonprofits with protection against spikes in unemployment claims, they do so at a cost. Much like SUTF, group trusts require employers to share the risk by spreading the cost of unemployment benefits among the group. Low-turnover nonprofits can still find themselves paying more than their own UI costs. Group trusts also resemble the taxable method in that many adopt membership payment formulas that are similar to an experience rating.

Unemployment Alternative Programs Provide Protection, Options

The two safest options for nonprofits are enrollment in an unemployment savings program or a bonded service program.

The two safest options for nonprofits are enrollment in an unemployment savings program or a bonded service program. The first program grants membership to a limited-liability corporation that provides access to professional claims management services and stop-loss insurance. The second, a bonded service program, employs first-dollar coverage plus the same excellent professional claims management services.

First Nonprofit Group can provide organizations with a savings analysis to determine if reimbursement financing is their best option for reducing UI costs. On average, First Nonprofit's Unemployment Savings Program LLC can save organizations up to 50 percent on their UI costs while bonded service program savings yields an average of 34 percent savings. Both programs also provide experienced claims management from industry professionals — with different levels of insurability — and audit services that reduce overpayments.

First Nonprofit Group Has Saved Organizations Thousands

The programs offered by First Nonprofit Group can save organizations of all sizes money on their UI costs.
Here are several examples:

- After enrolling in First Nonprofit Group's unemployment savings program, a mental health services center in Maryland with 114 employees reduced its UI costs by 22 percent, saving it more than $8,000 a year.

- A school in California saved $31,970 after membership in the First Nonprofit Group Limited Liability Corporation. The organization of 94 employees now pays a little more than $8,000 a year in UI costs, a savings of 79 percent compared to its costs in the State UI system.

- A Florida community mental health center with 259 employee saved almost $27,000 on UI costs after opting out of a state UI tax pool and joining the First Nonprofit Group savings program.

With the First Nonprofit Unemployment Savings Program, organizations pay an annual fee based on their own unemployment experience and don't have to worry about pooled risk. Unlike SUTF, the money that a nonprofit contributes to their interest-bearing reserve account with First Nonprofit Group belongs to the organization itself and can be carried on the balance sheet as an asset. The account balance is also returned to nonprofits if they should ever decide to leave the program.

Like the Unemployment Savings Program, nonprofits engaging in the Bonded Service Program receive an annual fee based on their own unemployment experience and don't have to worry about pooled risk. More importantly, the fee provides first-dollar coverage for all benefit charging for the life of the contract.

Deadlines are approaching for nonprofits that need to save money on UI costs for 2014 by opting out of unpredictable state tax pools. Contact First Nonprofit Group today for a no-obligation savings analysis and stop overpaying for unemployment insurance.

Deadlines for Saving On UI Costs Vary Among States

A written request to state unemployment agencies is due by November 30 in most states for nonprofits electing to finance unemployment claims under the reimbursing method for the upcoming tax year, New Hampshire, New York and Wisconsin must make their election by December 31. California and Minnesota nonprofits can make their election before the end of every quarter and Tennessee nonprofits have until May 31 of the same tax year.

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