

Back to the FUTA

No, this isn't about a movie.

This is an exercise to see how well you know the rules for FICA/FUTA withholding. FICA, or the "Federal Insurance Contributions Act" funds Social Security and Medicare. FUTA, or the "Federal Unemployment Tax Act," funds (this isn't rocket science ☺) unemployment benefits.

Social Security and Medicare (FICA)

Regardless of the amount employees contribute to Social Security and Medicare, employers are responsible for filing the entire tax. Once the total liability has been calculated and the correct amount subtracted from employees' paychecks, the remaining portion must be paid by the employer.

Social Security: 6.2%. Frequently labeled as OASDI (it stands for old-age, survivors and disability insurance), is withheld on the first \$160,200 of wages in 2023. Paying this tax is how a worker earns credits for Social Security benefits later.

Medicare: 1.45%. This tax pays for health insurance for people who are 65 or older, younger people with disabilities and terminal dialysis patients. Additionally, employers typically have to withhold an extra 0.9% on compensation over \$200K (single)/\$250K (MFJ).

Federal Unemployment Tax (FUTA)

Together with state unemployment insurance programs, employees who lose their jobs may be entitled to payments through the Federal Unemployment Tax Act. This tax cannot be deducted from employee wages, because it is solely an employer tax.

Identify whether FICA and FUTA taxes apply to each of the situations listed below:

- | | | |
|--|----------|---------|
| 1. Employer contributions to HSAs | Yes_____ | No_____ |
| 2. Employee contributions to Section 457 plans | Yes_____ | No_____ |
| 3. Employee 401(k) plan elective deferrals | Yes_____ | No_____ |
| 4. Employee contributions to FSAs | Yes_____ | No_____ |
| 5. Social Security retirement benefits | Yes_____ | No_____ |
| 6. Employee contributions to HSAs | Yes_____ | No_____ |
| 7. Distributions from nonqualified deferred compensation plans | Yes_____ | No_____ |
| 8. Distributions from IRAs | Yes_____ | No_____ |
| 9. Contributions to nonqualified deferred compensation | Yes_____ | No_____ |
| 10. Employer payments to Section 162 programs | Yes_____ | No_____ |
| 11. Employer matching contributions to 401(k) plans | Yes_____ | No_____ |
| 12. Earnings from a ROTH IRA | Yes_____ | No_____ |

ANSWERS:

1. Employer contributions to HSAs Yes _____ No X

Employer contributions to HSAs are not treated as compensation and are not subject to FICA/FUTA.

2. Employee contributions to Section 457 plans Yes X No _____

Employee contributions to 457 plans are treated as deferred compensation and thus are subject to FICA/FUTA.

3. Employee 401(k) plan elective deferrals Yes X No _____

Employee elective deferrals are subject to FICA and FUTA tax but not subject to ordinary income tax.

4. Employee contributions to FSAs Yes _____ No X

Salary reduction contributions to FSAs are not actually or constructively received by the participant. Therefore, those contributions are not considered wages for federal income tax purposes. In addition, they generally are not subject to FICA and FUTA.

5. Social Security retirement benefits Yes _____ No X

Retirees are not required to pay FICA taxes on many types of retirement income, including Social Security benefits, pensions, annuities, 401(k) distributions and IRA distributions. However, they can still expect to pay FICA taxes on earned income from a post-retirement job.

6. Employee contributions to HSAs Yes X No _____

Direct employee contributions to health savings account are subject to FICA and FUTA taxes unless the company has a section 125 cafeteria plan.

7. Distributions from nonqualified deferred compensation plans Yes X No _____

Under the special timing rule, deferred compensation is generally treated as wages for purposes of FICA taxes at the later of when the services are performed creating the right to the deferred compensation or when the deferred compensation is no longer subject to a substantial risk of forfeiture (i.e., upon vesting).

8. Distributions from IRAs Yes _____ No X

Taxpayers are not generally required to pay FICA/FUTA taxes on retirement plan distribution. This rule applies to both IRAs and qualified plans.

9. Contributions to nonqualified deferred compensation Yes _____ No X

When they are made, contributions to nonqualified deferred compensation arrangements are not subject to FICA or FUTA tax. Because of the substantial risk of forfeiture requirement to maintain the deferral, it is possible that the employee may never constructively receive the deferred compensation. However, when the substantial risk of forfeiture is lifted, the deferred compensation is subject to FICA/FUTA.

10. Employer payments to Section 162 programs

Yes X No

Section 162 arrangements represent a bonus in the form of life or disability insurance from an employer to retain a valued executive. As a bonus the employer-paid premium for the insurance that is given to the employee is treated as compensation subject to FICA and FUTA tax as well as to federal income tax. Certain employers may gross up the bonus to cover the employee's tax exposures.

11. Employer matching contributions to 401(k) plans

Yes No X

Employer matching contributions to 401(k) plans are not subject to FICA/FUTA tax when they are made or when they are distributed.

12. Earnings distributed from a ROTH IRA

Yes No X

Earnings from a Roth may be subject to income tax, but no withdrawals are subject to FICA or FUTA. The presumption is that Roth's are funded with taxable (non-deductible) dollars from which those taxes were taken out by an employer.