

### California and Virgin Islands Subject to Credit Reduction for 2025

According to the U.S. Department of Labor (DOL), *California* and the *U.S. Virgin Islands* did not pay back their federal loans by the November 10, 2025, deadline and will lose the full Federal Unemployment Tax Act (FUTA) credit for 2025 [DOL, [Final 2025 Federal Unemployment Tax Act \(FUTA\) Credit Reductions](#), rev. 11-10-25].

For 2025, California is subject to a FUTA credit reduction of 1.2% and the Virgin Islands is subject to a FUTA credit reduction of 4.5%. The Virgin Islands had a credit reduction in each of the past 14 years (2011-2024; see [PAYSTATE UPDATE, Issue 23, Vol. 26](#)).

#### Connecticut and New York paid off loans

In January, the DOL released its list of potential FUTA credit reduction states for 2025, including: California, *Connecticut*, *New York*, and the Virgin Islands (see [PAYSTATE UPDATE, Issue 2, Vol. 27](#)). Connecticut was not subject to a credit reduction for 2024. However, Connecticut had an outstanding loan balance on at least three consecutive January 1 (in 2022, 2023, 2024, and 2025). Therefore, it could have faced a credit reduction for 2025. Connecticut paid off its outstanding loans by the November 10, 2025, deadline and does not face a credit reduction for 2025 (it is listed in the DOL chart with a reduction amount of 0.0%).

New York was subject to a credit reduction of 0.9% for 2024. But earlier this year, the governor of New York announced that the state budget allocated money to pay off the state's federal unemployment account (FUA) loans. Since the state paid off the loans by the November 10, 2025, deadline and did not resume borrowing, it does not face a credit reduction for 2025 (see [PAYSTATE UPDATE, Issue 18, Vol. 27](#)). Like Connecticut, it is listed in the DOL chart with a reduction amount of 0.0%.

#### Credit reductions because of state loans

Under the joint federal/state unemployment insurance (UI) system, states with a high rate of unemployment and difficulty meeting their benefit obligations can borrow money from the FUA to pay benefits. If states have loan balances on January 1 of at least 2 consecutive years *and* on November 10 of the second year, the FUTA credits for employers in those states are reduced, with the extra FUTA tax paid being applied against each state's loan balance (see [The Payroll Source](#)®, §7.1-6).

A state with an outstanding loan can avoid a credit

reduction for its employers by repaying all outstanding loans by November 10 of the year the reduction is scheduled to take effect. If the loan is not repaid by that date, a credit reduction of 0.3% goes into effect, with employers in that state having their maximum credit reduced to 5.1% (5.4%–0.3%). The extra 0.3% in FUTA tax means that employers will have to pay an extra \$21 per employee (0.3% of the federal wage base of \$7,000). An additional credit reduction of 0.3% is taken for each additional year the loan remains unpaid.

Once a state/territory has had outstanding FUA loan balances for several years, additional types of credit reduction also might be added, including a 2.7% add-on and/or a Benefit Cost Rate (BCR) add-on. States/territories may apply to the DOL for a waiver of the BCR add-on by July 1 of a tax year. California was facing a BCR add-on of 3.4% for 2025, but the state applied for the waiver by the deadline, and it was approved. The Virgin Islands BCR add-on rate was 0%, based on the wages and tax contributions for calendar year 2024, but it is still listed as waiver approved for 2025.

#### Form 940, Schedule A will reflect reduction

The additional FUTA tax must be deposited by the due date of the 2025 federal Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, which is February 2, 2026 (because January 31, 2026, is a Saturday). The 2025 Schedule A (Form 940), *Multi-State Employer and Credit Reduction Information*, will contain the official list of credit reduction states, and the credit reduction total from Schedule A is reported on Form 940. The IRS has not released the final 2025 Form 940 yet. When they are finalized, both forms will be available on the IRS website and on the PayrollOrg website. To find the forms on the PayrollOrg website, select "News & Resources," then "Resource Library." Once in the Resource Library, check the box on the left side of the screen for "IRS Forms."

#### Outlook for 2026

As of November 6, California and the Virgin Islands continue to have outstanding loan balances. Both will face an increased credit reduction for 2026 if outstanding loans are not repaid by November 10, 2026. If Connecticut and New York resume borrowing and have outstanding loans on January 1, 2026, the DOL will consider Connecticut and New York potential credit reduction states for 2026. ■

### Massachusetts Supreme Court Rules Retention Bonuses Are Not Wages

The Supreme Judicial Court of *Massachusetts* ruled that a retention bonus was not considered wages under the state Wage Act [*Nunez v. Syncsort Inc.*, No. SJC-13709 (Mass.,

10-22-25)]. To be considered wages, a payment must be made in exchange for the employee's labor or services. Although a retention bonus may be partially in exchange for an

employee's labor, the court viewed the bonus as an exchange for an employee's loyalty to remain with the company.

### **Retention bonus paid after termination**

Syncsort Inc. is a data management software company. In 2020, Syncsort rebranded and merged with another business. Around the time of the merger, Syncsort hired Carlos Nunez as a full-time senior director of finance. However, a few months later, Syncsort changed Nunez's position to part time and reduced his salary. Nunez and Syncsort entered into a retention bonus agreement where Syncsort would pay him \$15,000 in two installments if he remained with the company until November 18, 2020, for the first installment and February 18, 2021, for the second. In addition, Nunez would have to remain employed with the company with no reduction in his work schedule and remain in good standing.

On February 18, 2021, Nunez was terminated as part of a reduction in force. Eight days later, on February 26, the company paid Nunez the second retention bonus installment. Nunez sued, claiming that the retention bonus was part of his wages and due on the same day as his termination. Under state law, when employees are involuntarily terminated, wages are due immediately.

### **Retention bonus compensates loyalty, not labor**

Because an employee who is terminated must be paid all wages on the day of termination, the question in this case was whether the retention bonus constituted a wage under the definition of the Wage Act.

The Supreme Judicial Court noted that not all forms

of compensation or benefits are wages. Wages specifically includes any holiday or vacation payments due and commissions (when the amount of the commission has been definitely determined and becomes due and payable). This is in addition to other forms of wages, such as hourly wages, piece-rate pay, or salary.

Commissions are the only contingent form of compensation that the Wage Act expressly allows. In prior cases, the court has ruled that other forms of contingent compensation are not wages, including: unused sick time, discretionary stock option plans, profit distribution under stock agreements, severance pay, equity under stock agreements, incentive signing bonuses, and other bonuses.

Nunez argued that the retention bonus payment should be considered part of wages because the payment is promised in exchange for his labor or services. However, the court characterized the retention bonus differently. Instead of compensating the employee for their labor or services (which would fall under the definition of a wage), the court viewed the bonus as compensation for Nunez's loyalty during a period of uncertainty with the company. The court notes an employee in Nunez's position may be tempted to leave the company due to the uncertainty, and the retention bonus helps to compensate the employee for foregoing other employment opportunities. The retention bonus was not solely made in exchange for Nunez's services, so the court held that the bonus was not a wage under the state Wage Act. ■

## **Additional States Offer Guidance Regarding OBBBA**

**A**dditional states issued guidance regarding H.R. 1, known as the One Big Beautiful Bill Act (OBBBA; Pub. L. 119-21). In some states, governors have called for special legislative sessions to address conformity with the OBBBA or to decouple state law from it. Learn more about updates in *Alabama, Delaware, Indiana, and Minnesota*.

It is important for payroll professionals to be aware of state laws and guidance in this area, as some states may follow certain provisions of the OBBBA and decouple from others. Previously, *California, Colorado, Maine, Massachusetts, Michigan, and Rhode Island* passed laws and/or issued guidance regarding OBBBA conformity (see [PAYSTATE UPDATE, Issue 21, Vol. 27](#)). More information on federal OBBBA requirements is available on [PayrollOrg's OBBBA Payroll Hot Topics](#) page.

### **Alabama does not conform to OBBBA**

The Alabama Department of Revenue's (DOR) guidance explains that the computation of Alabama personal income tax begins with state adjusted gross income [DOR, [The One Big Beautiful Bill Act Analysis and Tax Provisions](#), rev. 11-10-25]. This means that Alabama income tax is not directly tied to the calculation of federal taxable income. Alabama conforms to the current version of the Internal Revenue Code (IRC). But because there are currently no state laws regarding personal income tax deductions for

tips or overtime, the state is not currently following the "no tax on tips" and "no tax on overtime" provisions.

### **Delaware, Indiana governors call for tax law changes**

The governor of Delaware called the state legislature to convene a special session to address a projected \$400 million revenue shortfall over the next 3 years [Office of the Governor, [Press Release](#), 10-31-25]. The state follows the current version of the IRC, meaning it would follow the OBBBA. The governor supports a proposal to decouple the state from the federal tax law.

The governor of Indiana signed a proclamation calling a special legislative session to address the OBBBA [Office of the Governor, [Press Release](#), 10-27-25]. Indiana uses federal tax law as a starting point for state personal income taxes. However, the state conforms to the IRC as of January 1, 2023, and the OBBBA was signed on July 4, 2025. The governor supports changing IRC conformity date so that Indiana will conform to the OBBBA.

### **Minnesota does not conform to OBBBA**

The Minnesota Department of Revenue (DOR) has posted guidance explaining that the state conforms to the IRC as of May 1, 2023 [DOR, [2025 Federal Nonconformity for Income Tax](#), 11-3-25]. Therefore, it does not conform to the OBBBA. Draft personal income tax returns have been posted. ■