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Agenda

› Unemployment Insurance Review
› Introduction to M&A Implementation & Compliance
› Types of M&A Transactions
› State Compliance
› SUTA Dumping
› Payroll Integration
› Post-Implementation
› Takeaways
› Questions and Answers
UNEMPLOYMENT INSURANCE REVIEW
State repayment of Title XII loans can significantly impact an employer’s FUTA tax rates

FUTA Tax Review

<table>
<thead>
<tr>
<th>FUTA tax rate</th>
<th>FUTA taxable wage base</th>
<th>FUTA tax</th>
</tr>
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<tbody>
<tr>
<td>6.0%</td>
<td>$7,000</td>
<td>$420 Per Employee</td>
</tr>
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</table>

- If employer pays state SUI taxes timely and in full, a 5.4% credit is granted

<table>
<thead>
<tr>
<th>FUTA tax rate</th>
<th>FUTA tax credit</th>
<th>FUTA tax rate (less credit)</th>
<th>FUTA tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.0%</td>
<td>5.4%</td>
<td>0.6%</td>
<td>$42 Per Employee</td>
</tr>
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</table>

- If Federal Title XII loan remains outstanding for two years (as of January 1st), employers in the affected state lose 0.3% of the 5.4% credit (or $21 per employee)

- 0.3% FUTA credit loss continues for every year the Federal Title XII loan remains unpaid (Example: Year 1 = 0.3%; Year 2 = 0.6%, etc.)
Unemployment costs are impacted by several UI related activities

Missouri 2016 merit rating

A state example:

- Max: 9.75% (2015: 9.75%)
- Min: 0.00% (2015: 0.00%)

<table>
<thead>
<tr>
<th>Dollars</th>
<th>Reserve</th>
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<tbody>
<tr>
<td>State Taxes</td>
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<tr>
<td>Voluntary</td>
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<tr>
<td>Contributions</td>
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<tr>
<td>Administrative</td>
<td></td>
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<tr>
<td>Errors</td>
<td></td>
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<tr>
<td>Benefit Payments</td>
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</tbody>
</table>

- $13,000 Taxable wage base
- $1,268 Maximum Tax / employee
- $0 Minimum tax / employee
- $6,400 Maximum claim liability
INTRODUCTION TO M&A IMPLEMENTATION & COMPLIANCE
Effective M&A management begins with a comprehensive strategic planning process

**Due Diligence**
- Information and data gathering
  - Forms 940 and 941
  - Federal and state tax notices
  - UI tax rates and returns
  - Payroll policies and procedures
  - Past mergers and acquisitions
- Opportunity and risk assessment
  - High SUI tax rates
  - Unpaid employment taxes
  - "Payrolling"

**Planning and Design**
- Financial modeling and analysis
  - UI tax analysis
  - Successor wage base treatment: social security, FUTA, and SUI
  - Transfers of SUI experience: optional or mandatory
- Organizational and legal structuring
- Purchase agreement language

**Implementation and Compliance**
- Payroll integration
  - Compliance filings
    - Accounts registered and closed
    - Status changes
    - Account reconciliations
    - Benefit charge details
    - Payroll detail
    - Transfers of experience
    - Wage base transfers

**Post-Implementation**
- Realization of desired outcomes
  - Ensures timely processing of compliance filings
  - Coordination with state agencies to address inquiries
  - Confirm accuracy of successor tax rate calculations
  - Protest tax rate discrepancies
  - Verify tax accounts have been closed
  - Avoids the inefficient use of future resources
  - Shortens the time needed for accruing/budgeting revised tax rates
Effective M&A management is critical to unemployment cost minimization

Utilize cost management strategies
- Analyze transfer of experience options to obtain most favorable rate available
- Take advantage of Joint Account and Voluntary Contribution opportunities

Comply with federal and state rules and regulations
- Including P.L. 108-295; The SUTA Dumping Act of 2004
- Avoid loss of taxable wage base carryover
- Avoid notices and complications years after the transaction date

Proper processing of unemployment claims
- Ensure accurate payment of benefits to claimants
- Ensure benefit charges are assigned to the correct employer

Avoid penalties and interest
- Delinquent contributions
- Penalty rate
What is a Transfer of Experience (TOE)?

- **Transfer** – Movement of business operations (including employment), or portion thereof, from one legal entity to another, by any means; can involve asset-only or employee-only conveyances.

- **Experience** – History of factors used in the development of a UI tax rate over a specified period, including benefit charges, taxable payroll, and taxes paid.

- **Partial vs. Total** – two types of TOE both of which are mandatory between commonly owned, managed or controlled (“COMC”) legal entities.
TYPES OF M&A TRANSACTIONS
Employee Movements

» Internal Reorganizations
  ▪ Generally, anytime there are employees being moved or transferred from one affiliated legal entity to another.
  ▪ The decision to move or transfer the employee(s) is based on organization-wide initiatives versus employee-specific factors.
  ▪ Includes:
    – Transfers of a division, trade or business, or business unit
    – Job function follows the employee
  ▪ Excludes:
    – Promotions
    – Job reassignments

» External Acquisitions
  ▪ May take the form of a stock purchase, merger, or asset acquisition (including workforce) of an unaffiliated legal entity.
Basic Legal Entity Structure

Legal entities A & B are commonly owned by ParentCo.
Stock Acquisition of Legal Entity C

Considerations
- Stock acquisitions result in a change in the shareholder (owner)
- Underlying business is not impacted by the acquisition
Compliance – Stock

Jurisdictions will require updates to changes in:
- Owners
- Officers
- Address of Record
- Powers of Attorney

Payroll systems integration:
- Potentially different pay cycles with different employment tax liability deposit dates
- Proper calculation of taxable wage base limits
Subsequent Integration of Legal Entity C

Considerations

- Asset acquisitions typically involve the sale/purchase or a contribution of capital between two legal entities.
- After the transaction both legal entities continue to exist – seller/predecessor retains its legal identity.
- The acquisition will typically include the transfer (in whole or in part) of assets (including workforce) and select liabilities to the buyer/successor.
Compliance – Asset

- Employment tax registrations, status change notifications, TOE applications and account closures

- Form W-2 procedures (standard vs. alternate)

- Forms 940, 941, quarterly unemployment tax returns, annual reconciliations, including Schedule D

- Payroll systems integration:
  - Potentially different pay cycles with different employment tax liability deposit dates
  - Proper calculation of taxable wage base limits
Merger of Subsidiaries

Considerations

- A merger / consolidation is the combination of two or more legal entities into a single legal entity (e.g., the merger of two subsidiaries)
- The result of the transaction is only one legal entity survives
- Merger is a technical term relating to the combining of multiple legal entities often confused with other types of transactions
Compliance – Merger

› Employment tax registrations, status change notifications, TOE applications and account closures

› Required single Form W-2 filed by the survivor

› Forms 940, 941, quarterly unemployment tax returns, annual reconciliations, including Schedule D

› Payroll systems integration:
  ▪ Potentially different pay cycles with different employment tax liability deposit dates
  ▪ Proper calculation of taxable wage base limits
Other Considerations

► LLC Conversions
  - Different compliance requirements depending on the state:
    - Name change
    - Transfer of business

► Use of Employee Service Companies (ESC) or Employee Management Companies (EMC)

► Use of Intercompany Asset Leasing Arrangements

► Common Pay Agent and Common Paymaster

► Employee Management Contracts

► “Payrolling”: The improper practice of reporting the wages of one legal entity under the account of another legal entity
STATE COMPLIANCE
State Compliance Requirements

- It is the responsibility of the employer to **accurately** report a transaction to the state agencies.

Risks associated with non-compliance:

- If your organization is targeted for acquisition, improper compliance may impact acquisition terms.
- States utilize SUTA Dumping Detection Software ("SDDS") to monitor employee movements.
- Maximum rating and/or additional penalty rate for specified period.
- Civil and criminal penalties.
- Inability to carryover SUI taxable wage base limits.

Resource commitment:

- Complying with the requirements of 53 different taxing jurisdictions can be onerous and time-consuming.
- Confirm:
  - Compliance paperwork has or will be filed.
  - Accuracy of filings.
Other Considerations

» Timing of Transactions
  ▪ 12/31 vs. 1/1 vs. mid-year
  ▪ Issuance of revised rates
  ▪ Continuation of taxable wage base limits

» Forced UI Account Consolidations
  ▪ e.g., California, Indiana, Michigan, Oklahoma, & North Carolina

» Combined/Affiliated Rates
  ▪ e.g., Illinois & Texas
What if we are just moving a few employees?

- Differentiate between:
  - Employee specific reassignment or transfer
  - Employee reassignment or transfer based on business decision (e.g., transfer of specific business unit or function)
General State Successor Provisions

The transfer of a predecessor employer's UI experience to a successor employer is required if the predecessor employing unit transfers, through any means, all or part of the organization, trade, or business, to the successor employer and there is substantially common ownership, management or control of the entities.

The main purpose for these provisions is to provide the workforce agencies sufficient information to transfer the employer’s unemployment experience associated with the workforce being transferred, pursuant to The SUTA Dumping Prevention Act of 2004.
State Specific UI Tax Provisions

- State transfer methods include:
  - Percentage of total GROSS payroll transferred
  - Percentage of total TAXABLE payroll transferred
  - Percentage of EMPLOYEES transferred
  - Wage detail or specific identification for employees transferred

- When does the TOE become effective?
  - Immediately
  - First day of following quarter?
  - First day of current quarter?
  - First day of following year?

- The TOE can positively OR negatively impact rates

- States can sometimes take years to process a transfer

- Assess account consolidation risk
SUTA DUMPING
What is SUTA Dumping?

Manipulation of state experience rating systems, through a shift in workforce from one legal entity to another, so that employers pay lower state unemployment taxes than their unemployment experience would otherwise allow (i.e., obtaining “undeserved” lower tax rates).

The SUTA Dumping Prevention Act of 2004 focuses on:

- Transfers of experience between employers having common ownership, management or control; and
- Employers entering into transactions with the sole or primary purpose of lowering SUI tax rates.
What is SUTA Dumping? (Continued)

Many employers have been led to believe that there are no longer planning opportunities after the SUTA Dumping Prevention Act of 2004.

SUTA Dumping Defined: Illegal acts that are contrary to enacted state UI legislation originally mandated by the SUTA Dumping Prevention Act of 2004.

Often detected when:
- An employee files a claim under a different employer; or
- A group of employees (by SSN) is reported under a new/different employer.

The SUTA Dumping Prevention Act of 2004 is intended to prohibit certain perceived abuses.
Results of SUTADumping Detection

Source: U.S. Department of Labor
- Mandatory Transfers: State forced a transfer of experience as a result of transfers of workforce between legal entities
- Net amount charged to employers as a result of the forced transfer of experience
PAYROLL INTEGRATION
Payroll Integration Issues

» Form W-2 processing
  ▪ Single Form W-2 (required with merger/optional with asset purchase)
    – Less likely to duplicate employment taxes
    – Requires year-end account reconciliations
      • Federal Form 941 Schedule D
      • State Filings
      • 940 Best Practice – include cover letter with details of transaction
    – Employee “friendly” – no excess FICA tax, single Form W-2

  ▪ Two Forms W-2 (only available with asset transfer and internal reorganization)
    – Doesn’t require complete YTD wage information from predecessor
    – Still requires YTD wage base information from predecessor to avoid wage base duplication
    – Not employee “friendly”
Payroll Integration Issues

Common integration issues

- Conforming policies and procedures
  - SUI sourcing
  - Multi-state withholding
- Document reissue/transfer—Forms W-4, I-9, etc.
- Explore system and compliance “tricks and workarounds” to minimize workload

Considerations if using third party administrators

- Successor employer options not always available
- Year end account reconciliations
  - Federal Forms 940 and 941 Schedule D
  - State filings
- Mid-quarter state unemployment tax returns
- Mid-year wage base continuation
Wage Base Carryovers

**Federal**
- Wages paid by the predecessor can be used by a successor for purposes of the annual wage limitation (FICA and FUTA), if:
  - The successor acquired property used in a trade or business, or a separate unit of a trade or business, of the predecessor;
  - Predecessor employees were employed by the successor immediately after the acquisition; and
  - The wages were paid during the calendar year in which the acquisition occurred and prior to the acquisition.

  “Use of assets” doctrine

**State**
- Wages paid by the predecessor can be used by a successor for purposes of the annual wage limitation, if proper compliance documents have been filed and approved by the state workforce agencies.
Quantifying a Wage Base Restart

An employee earns $120,000 per year

<table>
<thead>
<tr>
<th>Tax Type</th>
<th>Wage Base (2015)</th>
<th>Tax Rate</th>
<th>Taxable Wages Employer A 1/1-6/30</th>
<th>Taxable Wages Employer B 7/1-12/31</th>
<th>Excess Taxable Wages</th>
<th>Refund Available</th>
</tr>
</thead>
<tbody>
<tr>
<td>FICA</td>
<td>$118,500</td>
<td>6.2%</td>
<td>$60,000</td>
<td>$60,000</td>
<td>$1,500</td>
<td>$93</td>
</tr>
<tr>
<td>FUTA</td>
<td>$7,000</td>
<td>0.6%</td>
<td>$7,000</td>
<td>$7,000</td>
<td>$7,000</td>
<td>$42</td>
</tr>
<tr>
<td>Texas SUI</td>
<td>$9,000</td>
<td>6.79%</td>
<td>$9,000</td>
<td>$9,000</td>
<td>$9,000</td>
<td>$611</td>
</tr>
</tbody>
</table>
Other Considerations

- Most states allow refund claims from three to five years after the initial filing and payment of tax.

- Out of state wage credits

- Upgraded SUI Reporting Systems.
  - Often do not provide the ability to obtain credit for wages paid to another state.
  - Creates discrepancy between state and employer calculations.
  - Certain states require employers to remit the entire UI tax due and subsequently report out-of-state wages to obtain a refund of the overpaid UI tax.
  - Certain states (i.e., LA and MN) will not give credit for wages paid to another state.
POST-IMPLEMENTATION
Why is Post-Implementation Important?

▷ Avoids the inefficient use of resources

▷ Shortens the time needed for accruing or budgeting revised tax rates

▷ Allows for the next M&A transaction to be implemented without concern

▷ Updates systems for legal entity structure changes that will impact the claims management program

▷ Realization of Desired Outcomes
How to Realize Desired Outcomes

 › Monitor status of compliance filings
   ▪ Communicate with state workforce agencies to assure paperwork has been received and is being processed accurately
   ▪ Delays in processing may lead to improper payment of taxes
   ▪ May have to manage as many as 53 different workforce agencies
   ▪ Avoids inquiries from state workforce agencies

 › Verify rate transfers
   ▪ Avoid unexpected retroactive rate revisions
   ▪ Avoid unexpected rate assignments because state does not follow statutes (e.g., transaction date of 12/31 versus 1/1)

 › Protest incorrect rates
UNEMPLOYMENT COST MANAGEMENT STRATEGIES
Voluntary contributions can be an effective strategy in reducing unemployment taxes

Additional considerations

- Employee population
- Mergers, acquisitions or reorganizations
- Multiple bracket reductions
- Expected increases and decreases in taxable payroll

States Allowing Voluntary Contributions

<table>
<thead>
<tr>
<th>State</th>
<th>State</th>
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<tbody>
<tr>
<td>Arkansas</td>
<td>Massachusetts</td>
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<td>Wisconsin</td>
</tr>
<tr>
<td>Louisiana</td>
<td>New Jersey</td>
<td>West Virginia</td>
</tr>
<tr>
<td>Maine</td>
<td>New York</td>
<td></td>
</tr>
</tbody>
</table>
Equifax reduces unemployment taxes through strategic joint account (common rating) planning

**Planning and design**
- Define states allowing Joint Account option
- Review legal entity structure
- Evaluate unemployment tax savings
- Analyze all possible rate combinations
- Compliance requirements
  - Review of state statute
  - Duration and filing deadlines
  - Dissolution provisions
  - Common ownership definitions

**Implementation**
- File compliance documents timely

**Post implementation**
- Verification of combined tax rate assignments
- Protest of incorrect determinations
- Validation of tax savings achieved
- Annual review for dissolution and modification
TAKEAWAYS
Takeaways

› It is the responsibility of the employer to report the transaction

› Avoid risks associated with:
  ▪ Compliance requirements
  ▪ Potential penalties
  ▪ Claims management program
  ▪ Payroll tax return filings (Forms W-2, etc.)
  ▪ Not reporting small groups of employees

› Take advantage of opportunities:
  ▪ Available transfer of experience options
  ▪ Voluntary contributions
  ▪ Joint accounts
  ▪ Wage base carryovers

› Be prepared with the necessary resources (including follow-up)
Questions and Answers

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