Buchalter
COVID-19 Alert

March 19, 2020

Tax credits to offset Congress' newly-mandated paid leave

On March 18, 2020, President Trump signed into law the bipartisan Families First Coronavirus Response Act (H.R. 6201) (the "**Act**"). H.R. 6201 requires employers with fewer than 500 employees to provide qualifying employees (as defined in the Act) with (1) emergency paid sick leave for certain specified reasons related to COVID-19; and (2) emergency paid family and medical leave for employees who are unable to work (or telework) because they need to care for children under 18 years of age whose school or place of care has been closed.

To mitigate the cost to employers of the Act's mandated paid sick and family leave, the Act also provides for a refundable payroll tax credit that employers can use to cover the cost of the mandated paid sick and family leave. Self-employed individuals may also benefit from a similar, refundable tax credit. The effective date will be on or before April 2.

The following discussion contains a brief summary of the parameters of the mandated emergency paid sick and family leave, followed by an explanation of the tax credits created to offset the cost of mandated leave to employers.

Summary of Mandated Paid Sick and Family Leave

Under the Emergency Paid Sick Leave Act (which is a component of the Act), employers must provide full-time employees 80 hours (10 days based on an 8-hour workday) of paid sick leave. (For part-time employees, the number of hours required to be offered by an employer equals the average hours worked over a 2-week period.) If the employee takes sick leave to attend to his or her own health, the employer must cover all of the employee's wages, up to $511 per day. If the employee is caring for another person, the employer must cover two-thirds of the employee's wages, up to $200 per day.

Under the Emergency Family and Medical Leave Expansion Act (which is a component of the Act), employers must offer family leave for a period of up to 12 workweeks (*i.e.* , twelve 5-day periods) to employees needing to care for children whose school or place of care has been closed due to COVID-19. The employer must cover two-thirds of the employee's wages, up to $200 per day. The first 10 days (*i.e.* , first 2 workweeks) may be unpaid, although an employee can utilize emergency paid sick leave during that period, subject to a daily $200 limitation.

For a more detailed discussion of the paid sick and paid family leave mandates, please see the March 19, 2020 Buchalter COVID-19 Alert – "Employment Legislative Actions in the Works Following the COVID-19 Outbreak."

Overview of Refundable Payroll Tax Credits

Credits for Employers

The Act provides payroll tax credits to employers to offset wages required to be paid by the employer as (1) "qualified sick leave wages" under the Emergency Paid Sick Leave Act and (2) "qualified family leave wages" under the Emergency Family and Medical Leave Expansion Act, in each case subject to applicable duration and amount limitations. These limitations cap the "wages" element of the credits.

Each credit is increased (without limitation) by the amount of qualified employer-paid health insurance plan premiums and expenses ("**qualified health plan expenses**"), that are properly allocated to qualified sick leave wages or qualified family leave wages. The allocation method will be described by future regulations. Until these regulations are issued, employers may allocate qualified health care expenses pro rata among covered employees and based on periods of coverage. The total credit available per employee is equal to the maximum qualified sick leave and family leave wages described above plus all properly allocated qualified health plan expenses. For example, the maximum paid sick leave credit amount per employee on leave to care for himself or herself is the sum of $5,110 (*i.e.*, $511 per day for 10 days) plus the amount of qualified health plan expenses allocated to the period of leave.

These credits generally may only be applied against the employer's portion of the Social Security tax component of FICA payroll tax. However, if the aggregate amount of an employer's (1) qualified sick leave wages, (2) qualified family leave wages, and (3) properly allocated qualified health plan expenses exceeds the employer's Social Security payroll tax liability for the specified period (generally each calendar quarter), then this excess amount generally will be refunded to the employer, even if no payroll tax is paid for that period.

The tax credit will be included in the employer's gross income, and the payment of wages and health insurance will remain deductible under existing rules.

Credits for Self-Employed Individuals

The Act provides self-employed individuals with credits analogous to those provided to employers for emergency paid sick leave and emergency paid family leave. By contrast to employer credits, credits for self-employed individuals may be used to offset income and self-employment payroll taxes.

Instead of using "wages" as a benchmark, both credits for self-employed individuals define "average daily self-employment income" as "the net earnings from self-employment income of the individual for the taxable year, divided by 260." The benefit calculation for each credit under the self-employed individual scenario is similar to the calculation described above applicable to employers, utilizing average daily self-employment income in lieu of wages. Limitations on the credits for self-employed individuals are similar to that of the credits for employers.

How to Utilize the Credit

Payroll taxes, such as FICA taxes and withheld income taxes, are reported by employers for all their employees on the same return, which generally is IRS Form 941, *Employer's Quarterly Federal Tax Return*. For each quarter, the employer should:

1. Calculate its payroll tax liability.

2. Calculate the aggregate amount of qualified sick leave wages and qualified family leave wages paid to covered employees.

3. Calculate the maximum credit allowed for wages paid to all covered employees. (While this is a 100 percent credit, it is 100 percent of the maximum benefit amount as set forth in the Act for each type of paid leave.)

4. Calculate the aggregate amount of qualified health plan expenses.

The sum of the wages paid amount plus the amount of employer-paid health insurance premiums and expenses is the credit amount for the relevant quarter. Employers should apply the credit against its payroll tax liability for that quarter. The excess (if any) will be treated as an overpayment and paid to the employer as a refund.

Self-employed individuals should utilize similar steps to calculate their maximum allowable leave benefits. Self-employed individuals should apply any credit available against their estimated income tax payments and will receive a payment of the excess as a refund.

If we can be of assistance and to discuss various options and specific situations, please feel free to contact any of the Buchalter Tax, Benefits, and Estate Planning attorneys below.

Philip J. Wolman
Shareholder
(213) 891-5390 or
pwolman@buchalter.com

Christopher Luna
Attorney
(213) 891-5416 or
cfurby@buchalter.com

Tonie L. Bitseff
Special Counsel
(206) 319-7042
tbitseff@buchalter.com

Gerald "Jerry" Janoff
Senior Counsel
(213) 891-5206 or
gjanoff@buchalter.com

Stuart A. Simon
Of Counsel
(213) 891-5019 or
ssimon@buchalter.com