MAY 2018
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BDO KNOWS: COMPENSATION AND BENEFITS

SUBJECT

IRS ISSUES GUIDANCE TO EMPLOYERS ON THE PAID FAMILY LEAVE TAX CREDIT

SUMMARY

The Tax Cuts and Jobs Act, signed into law in December 2017, created a new business credit for employers that offer paid family and medical leave under new Section 45S. The IRS released initial guidance in the form of FAQs for this employer tax credit.

DETAILS

Eligible employers

An eligible employer is one that has a written policy that provides at least two weeks of annual paid family and medical leave to qualifying employees who work full-time (and prorated for employees who work part-time).

Qualifying employees

A qualifying employee is any employee who has been employed by the employer for one year or more, and who for the preceding year, had compensation not more than 60 percent of the threshold for a highly compensated employee. Thus, for an employer claiming a credit for wages paid to an employee in 2018, the employee must not have earned more than $72,000 in 2017.

Qualifying leave

The tax credit is available for an employer's paid family and medical leave program that provides wage replacement to employees who need time away from their jobs for one or more of the following reasons:

- To care for a newly born, adopted or fostered child;
- To care for the employee's spouse, child or parent with a serious health condition;
- For a serious health condition that makes the employee unable to perform the functions of his or her position;
- To assist loved ones when a spouse, child, or parent is deployed on active military service; or
- To care for a service member who is the employee's spouse, child, parent or next of kin.

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An employer may not claim the credit for paid leave provided under the employer's vacation or personal leave policy, or other medical or sick leave that does not satisfy the purposes stated above. In addition, any leave paid by a state or local government, or required by state or local law, is not eligible for the credit.

Amount of the credit

The credit is equal to 25 percent of the amount of wages paid to a qualifying employee while on family and medical leave. The paid leave must equal at least 50 percent of the employee's regular wages. The credit is available for up to 12 weeks of paid family and medical leave per taxable year.

Interaction of the paid family leave tax credit with deductions and other wage-based tax credits

An employer must reduce its deduction for wages or salaries paid or incurred by the amount determined as a credit. In addition, any wages taken into account in determining any other general business credit (e.g., the Worker Opportunity Tax Credit or any applicable disaster relief employee retention tax credit) may not be used in determining the paid family and medical leave tax credit.

Temporary availability of the credit

The credit is generally effective for wages paid during the employer's taxable years beginning after December 31, 2017, and is not available for wages paid in taxable years beginning after December 31, 2019.

BDO INSIGHTS

The federal paid family and medical leave program is voluntary and employers are not required to maintain such policy. Employers considering adopting the program should assess the benefits, costs and impact on other leave programs.

The paid family and medical leave program provides wage replacement to employees who need time away from their jobs for exigent circumstances. Such program may increase talent retention, recruitment, and employee appreciation. However, there are increased employer costs to maintaining the paid leave program, which is generally funded by the employer's assets (rather than employee contributions or insurance carriers). If an employer adopts a paid family and medical leave program for the first taxable year beginning after December 31, 2017, the federal government will share 25 percent of the wages paid under the program for only two years. While the tax credits expire after the two-year period, the paid family and medical leave program itself may not be easily terminated in light of employee expectations. In absence of the federal subsidy, employers would incur additional costs for this ongoing program.