Is the New FMLA Tax Credit Worth It?

McGlinchey Labor & Employment Alert

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Employers who pay employees while they are on Family and Medical Leave Act (FMLA) leave can receive a new tax credit under new Internal Revenue Code Section 43S, but the limitations on the applicability of the credit may make this tax deal more trouble than it is worth.

How generous is the credit?
If employees are paid 100% of their normal wages or salaries, the credit is 25% of that pay. The credit reduces pro rata based on percentages of pay less than 100% to a floor of 12.5% if the paid leave is 50% of normal pay.

How long does the paid FMLA leave have to last?
To get the credit, the employer must offer a minimum of two weeks of paid FMLA leave. The maximum paid time off eligible for the credit is 12 weeks, which is the maximum FMLA leave mandated by law.

Which employees have to be offered the paid leave?
Both full-time and part-time employees have to be offered the paid FMLA leave for the employer to be eligible for the credit, although the duration of the paid leave that must be offered to part-timers is reduced pro rata based on their work schedules compared to full-time. No guidance has been issued by the IRS as to whether the benefit can be limited to certain classes of employees or whether the benefit must be universally offered. In addition, the credit does not apply unless the employee on leave has been employed for at least a year and did not earn more than $72,000 in the preceding year.

Does paid time off used for FMLA count?
No. The law specifically provides: "If an employer provides paid leave as vacation leave, personal leave, or medical or sick leave … that paid leave shall not be considered to be family and medical leave" unless the paid leave is specifically for time taken for an FMLA leave. Thus, until paid time off that may be applied against FMLA leave is exhausted, the credit will not apply. Similarly, if the paid FMLA time off is being provided in compliance with a state law that mandates paid medical or family leave, the credit is unavailable for that time off.

Can the credit be claimed without a formal paid FMLA policy?
No. The credit only applies if the paid time off is being paid pursuant to a written policy that promises at least two weeks of this paid time off for FMLA leave for eligible full- and part-time employees.

What if FMLA does not apply?
If an employee’s leave was not technically covered by FMLA, such as leave taken by an employee who worked at a site with fewer than 50 employees or a part-time employee who did not work sufficient hours to be eligible for FMLA, the credit is still available; however, the employer’s written paid FMLA leave policy must provide job protection for the employee taking the leave and must provide the employee with anti-retaliation and anti-discrimination protections for exercising the employee’s rights under the leave policy. Because the requirement that the employer’s paid FMLA time off must be offered to part-timers, many of whom would normally not qualify for actual FMLA leave, it appears that all employers’ paid FMLA leave policies will have to contain these additional legal protections for such employees.

How long is this credit available?
The credit only applies with respect to eligible leave taken after 2017 but before 2020, when the law sunsets.

Is the credit worth it?
Bottom line, the cost of offering paid FMLA leave on top of the paid leave available by applying paid sick or vacation leave towards FMLA leave, combined with the costs imposed by the need to offer paid leave to part-timers and to guarantee them job protection after the leave is taken, may make the tax credit unappealing for many employers.

However, if an employer wants to provide extra paid leave as a benefit for valued employees, employers should ensure that they adopt a compliant written policy so that the employer can take advantage of this new tax credit.

For more information regarding this alert, please contact a member of the firm’s Labor & Employment Team.