Tax Alert: What Employers and Self-Employed Individuals Need to Know About the Coronavirus Response Act Tax Credits for Emergency Paid Leave

March 23, 2020

On March 18, 2020, President Trump signed the Families First Coronavirus Response Act (the "Act") into law. The Act requires employers with less than 500 employees and certain public employers to provide Emergency Paid Sick Leave and Paid FMLA Leave (Public Health Emergency Leave) to their employees who miss work for various reasons related to COVID-19. To help offset the cost for employers who are required to pay these new leave benefits, the Act provides these employers with certain payroll tax credits. This alert explains the new payroll tax credits and how employers can utilize the credits to help offset the cost of any paid leave benefits they are required to pay to their employees under the Act. This alert also describes how certain self-employed individuals can take advantage of the new credits offered under the Act.

Overview of Emergency Sick Leave and Paid FMLA Payments

The Emergency Paid Sick Leave provision of the Act allows employees up to 80 hours of paid sick leave. If the employee is sick, the employee receives the lesser of the employee's regular pay rate or $511 per day. If the employee is taking care of someone else who is sick or if the employee's child's school is closed, the employee receives the lesser of two-thirds (2/3) of the employee's regular wages or $200 per day. The Paid FMLA Leave provision of the Act entitles employees to the lesser of two-thirds (2/3) of their regular pay rate or $200 per day for a period of up to 10 weeks, with a maximum of $10,000.

To learn more about employee eligibility requirements for both types of leave, see this Lathrop GPM Legal Alert (https://www.lathropgpm.com/newsletter-72493.html).

Tax Credits for Emergency Paid Sick Leave

To help employers offset the cost of providing paid leave, the Act provides employers with a refundable payroll tax credit for each calendar quarter equal to 100% of the Emergency Paid Sick Leave paid with respect to such quarter. Employers may claim the credit for no more than 10 days of Emergency Paid Sick Leave per employee. The credit is also available to the employer for qualified health plan expenses allocable to Emergency Paid Sick Leave for which the credit is allowed, but only to the extent the qualified health plan

expenses are excludable from gross income of the employee.

The credit is to be claimed against the employer's 6.2% share of the Old Age, Survivors, and Disability Insurance (OASDI) tax due for the quarter (but see the discussion below regarding IRS guidance, which may allow the credit to be claimed against other taxes). To the extent that the credit exceeds the employer's portion of the OASDI tax due, the excess is refundable to the employer.

The Emergency Paid Sick Leave paid by an employer is not subject to the employer's 6.2% share of the OASDI tax. Employers must continue withholding employee portions of OASDI and Medicare taxes.

The credit does not apply to the federal government, the government of any state or any subdivision of a state, or any agencies or instrumentalities of these entities. Employers can also elect to not apply the new credit provision during any calendar quarter.

Tax Credits for Paid FMLA Leave

Similarly, the Act provides employers with a refundable payroll tax credit equal to 100% of the Paid FMLA Leave, not to exceed $10,000 per employee. The credit is also available to employers for qualified health plan expenses allocable to Paid FMLA Leave for which the credit is allowed.

The credit is to be claimed against the employer's 6.2% OASDI tax due for the quarter (but see the discussion below regarding IRS guidance, which may allow the credit to be claimed against other taxes). To the extent that the credit exceeds the employer's portion of the OASDI tax, the excess is refundable to the employer.

The Paid FMLA Leave paid by an employer is not subject to the employer's 6.2% share of the OASDI tax. Employers must continue withholding employee portions of OASDI and Medicare taxes.

The credit does not apply to the federal government, the government of any state or any subdivision of a state, or any agencies or instrumentalities of these entities. Employers can also elect to not apply the new credit provision during any calendar quarter.

Denial of Double Benefits

To prevent employers from receiving a double benefit in the form of a credit and a deduction, the Act requires employers to include in gross income the amount of any credits they claim. Any credits employer claim under the Act will not be taken into account when the employer determines the amount of Section 45S family and medical leave credit to which it may otherwise be entitled.

Tax Credits for Self-Employed Individuals

Self-employed individuals may also claim an equivalent refundable credit against their income taxes for both types of leave. To qualify, self-employed individuals must regularly carry on a trade or business as defined by section 1402 of the Internal Revenue Code, and they must also demonstrate that their circumstances would have qualified them to take Emergency Paid Sick Leave or Paid FMLA Leave if they had been employed as an employee of an employer other than themselves. Self-employed individuals are subject to the same limitations as employers for the number of total days they may claim either tax credit.

To calculate a self-employed individual's equivalent tax credit for Emergency Paid Sick Leave because the employee is sick, the individual multiplies the number of days he or she is unable to work and would have been entitled to take leave by the lesser of $511 or their "average daily self-employment income." The average daily self-employment income is the individual's annual net self-employment earnings for the tax year divided by 260.

For determining a self-employed individual's equivalent tax credit for Paid FMLA Leave or Emergency Paid Sick Leave taken to care for another person or because the individual's child's school is closed, the individual multiplies the number of days of leave taken by the lesser of $200 or 67% of the individual's average daily self-employment income.

Effective Date

The new tax credit provisions apply beginning on a date the Treasury Secretary or his delegate prescribes, which must be no later than fifteen days after enactment of the Act. The new tax credit provisions will expire on December 31, 2020.

When the new tax credit provisions go into effect, there will be a 30-day period of non-enforcement for good faith compliance efforts for employers reporting income and claiming the new tax credits.

Prompt Payment of Paid Sick Leave and Family Leave

According to an IRS news release published late last week, to ensure prompt payment of paid leave in the event employers are unable to cover the cost of paid leave under the Act, the IRS will issue guidance providing that employers may retain from employee paychecks federal income taxes and employer and employee shares of Social Security and Medicare taxes that employers would otherwise deposit with the IRS. An employer may withhold these additional payroll taxes only to the extent necessary to cover the cost of paid leave.

Under the anticipated guidance, if employers do not have sufficient payroll taxes to cover the cost of Paid Sick Leave and Paid FMLA Leave, employers may request an accelerated payment from the IRS. The IRS

anticipates processing these requests in two weeks or less.

In its news release, the IRS stated it will release additional guidance and details about these new procedures this week.

If you have questions about these new payroll tax credits, please contact Tom McMahon, Dave Bahls, Kyle Hertel, or your regular Lathrop GPM contact.