



# COMPLIANCE BULLETIN

## HIGHLIGHTS

- Employers of all sizes may qualify for the credit, even employers that are not subject to the federal FMLA.
- For 2018 tax years, employers may retroactively adopt written policies for paid family and medical leave.
- Amounts paid by a state or local government (or required by state or local law) do not qualify for the credit.

## IMPORTANT DATES

### 2018 and 2019

The tax credit applies to wages paid in taxable years beginning after Dec. 31, 2017. It does not apply to wages paid in taxable years beginning after Dec. 31, 2019.

## IRS Issues Guidance on Tax Credit for Paid Family and Medical Leave

### OVERVIEW

The IRS recently released [Notice 2018-71](#), which provides detailed guidance in question and answer (Q&A) format on the employer tax credit for paid family and medical leave. The tax credit is contained in [Section 45S](#) of the Internal Revenue Code (Code) and applies for 2018 and 2019 tax years.

The IRS' Q&As address the following topics:

- ✓ Eligible employers;
- ✓ Family and medical leave;
- ✓ Minimum paid leave requirements; and
- ✓ Calculating and claiming the credit.

This IRS guidance applies to taxable years beginning after Dec. 31, 2017, and before Jan. 1, 2020. The IRS also intends to issue proposed regulations on the tax credit in the future.

### ACTION STEPS

Employers that want to take advantage of the new tax credit should review the IRS' Q&As and work with their tax advisors, as necessary, to make sure they satisfy all of the applicable requirements for the tax credit.

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## Overview of Tax Credit

The employer tax credit for paid family and medical leave is calculated based on a **percentage of wages** that are paid to qualifying employees for paid family and medical leave. The percentage amount, which begins at 12.5 percent and is capped at 25 percent, increases by .25 percent for each percentage point by which the rate of payment for paid family and medical leave exceeds 50 percent of the employee's normal wages.

An eligible employer may only claim the tax credit with respect to paid leave that is taken for a purpose permitted under the federal Family and Medical Leave Act (FMLA). To be eligible for the tax credit, an employer must have a **written policy** in place that meets the following requirements:

*In general, an employer's written policy must be in place before the paid family and medical leave is taken in order to claim a tax credit for the leave. However, employers may retroactively adopt their written policies for 2018.*

<b>Qualifying Employees</b>	The employer must provide paid family and medical leave for <b>all qualifying employees</b> . A qualifying employee is an employee who has been employed by the employer for one year or more and, for the preceding year, had compensation not in excess of a specified amount (\$72,000 for 2017).
<b>Amount of Paid Leave</b>	For full-time employees, the leave policy must provide <b>at least two weeks</b> of annual paid family and medical leave. For part-time employees, who are defined as employees who are customarily employed for fewer than 30 hours per week, the leave policy must provide an amount of paid leave that is proportionally equal to the amount provided to full-time employees.
<b>Payment Rate</b>	The policy must require a rate of payment for paid family and medical leave that is not less than <b>50 percent</b> of the employee's normal wages.
<b>Employee Protections</b>	If an employer has any non-FMLA eligible employees, the policy must incorporate certain <b>non-interference protections</b> .

## IRS Guidance

The IRS' Q&A guidance addresses a variety of topics related to the employer tax credit for paid family and medical leave. Key points on these topics are summarized below.

### **Eligible Employers**

Any employer is eligible to claim the tax credit if it has a written policy in place that meets the requirements summarized above, even if the employer is not subject to the FMLA. In general, an employer's written policy

must be in place **before** the paid family and medical leave for which the employer claims the tax credit is taken.

A special transition rule applies for the employer's first taxable year beginning after Dec. 31, 2017. Under this rule, an employer's written leave policy (or an amendment to a policy) can be **adopted retroactively** if the policy is adopted on or before **Dec. 31, 2018**, and the employer brings its leave practices into compliance with the terms of the retroactive policy (or retroactive amendment), including making any retroactive leave payments, no later than the last day of the taxable year.

Also, an employer is not required to notify its employees about its written policy for paid family and medical leave. However, if an employer provides this notice, it must communicate the information in a manner reasonably designed to reach each qualifying employee. This may include, for example, email communication, use of internal websites, employee handbooks or posters in employee work areas.

## ***Family and Medical Leave***

As a general rule, paid leave can be used for claiming the tax credit only if it:

- ✓ Is for one or more FMLA purposes;
- ✓ Cannot be used for any other reason (such as vacation or personal leave); and
- ✓ Is not paid by a state or local government (or required by state or local law).

**Key point:** Any leave paid by a state or local government (or required by state or local law) is not taken into account in determining the amount of paid family and medical leave provided by the employer, the rate of payment under the employer's written policy or the determination of the tax credit.

Paid leave provided under an employer's **short-term disability program** (whether self-insured by the employer or provided through an insurance policy) may qualify as paid family and medical leave if it meets all of the applicable requirements of Code Section 45S.

## ***Minimum Paid Leave Requirements***

An employer's written policy may not exclude any classification of employees (for example, collectively bargained employees) if they are qualifying employees. However, an employer's rate of payment or period of paid family and medical leave does not have to uniform with respect to all qualifying employees or for all FMLA purposes.

## ***Calculating the Credit***

The credit is equal to the applicable percentage of the amount of wages normally paid to a qualifying employee during any period (up to 12 weeks) that he or she is on family and medical leave. Wages paid by a third party (such as an insurance company or professional employer organization) may be taken into account by the eligible employer for purposes of the tax credit.

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An employer may not claim the credit for wages paid to an employee who is not a qualifying employee when the family or medical leave is taken but who becomes a qualifying employee later during the tax year.

The credit is claimed on Form 8994, Employer Credit for Paid Family and Medical Leave, and reported on IRS Form 3800, General Business Credit. An employer must reduce its deduction for wages or salaries paid or incurred by the amount determined as a credit.