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New Tax Law Provides Employer Tax Credit for Compensation Paid to Employees While on Family and Medical Leave

February 1, 2018
Insights for Employers

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Service Areas

Labor & Employment

The new federal tax law, signed by President Trump in December, contains a number of provisions that will impact the workplace and employers. In a previous alert, we described how the new tax law eliminated the ability to claim a deduction for confidential sexual harassment or sexual abuse settlements. Today, we describe changes to the Family and Medical Leave Act (FMLA). (As many are aware, FMLA requires employers to provide certain employees with up to 12 weeks of job-protected leave annually for specified family and medical reasons. The leave may be paid or unpaid.)

To encourage employers to provide eligible employees with paid leave under FMLA, the new tax law provides eligible employers with a new business credit equal to 12.5% of the amount of wages paid to "qualifying employees" during any period in which such employees are on family and medical leave as long as the rate of payment under the program is at least 50% of the employee's normal wages. The credit increases from 12.5% by 0.25 percentage points (but not above 25% of wages) for each percentage point by which the rate of payment exceeds 50%. The credit can be used to lower an employer's taxable income, subject to limitations, and applicable alternative minimum tax. The amount of paid family and medical leave used to determine the tax credit for an employee may not exceed 12 weeks.

To be eligible for the credit, an employer must have a written policy that provides all qualifying full-time employees with at least two weeks of annual paid family and medical leave. Part-time employees are also to be allowed a commensurate amount of leave on a pro rata basis. Qualifying employees are those who have worked for the company for at least one year and were paid no more than 60% of the compensation threshold for highly compensated employees in the previous year. (For 2018, 60% of the compensation threshold is equal to 60% x $120,000 = $72,000.)

For purposes of the credit, any leave paid for by a State or local government or required by State or local law shall not be taken into account in determining the amount of paid family and medical leave provided by the employer. For example, if a jurisdiction, such as Chicago has an ordinance that provides paid sick leave for FMLA-permitted purposes, an employer will not qualify for the business tax credit if the paid leave is provided to be in compliance with the ordinance. As a result, it is important that the employer have a clear policy in place.

The Secretary of Treasury will determine whether an employer or an employee satisfies applicable requirements for the employer to be eligible for the tax credit based on information provided by the employer as the Secretary determines to be necessary or appropriate.

If the employee takes a paid leave for other reasons, such as vacation leave, personal leave, or other medical or sick leave, this paid leave will not be considered to be family and medical leave for purposes of the credit.

The credit is effective for wages paid in taxable years starting on January 1, 2018. It is set to expire for wages paid in taxable years beginning after December 31, 2019.

Questions

If you have any questions regarding the new tax credit for paid FMLA, contact Lisa Burman at 312-704-3832 or lburman@hinshawlaw.com, or your regular Hinshaw employment attorney.

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