

# Employee Benefit ■ Plan Review

## IRS Releases Guidance on Employer FMLA Tax Credit

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The Tax Cuts and Jobs Act (the Act), provides a temporary corporate federal tax credit, ranging from 12.5 percent to 25 percent, that may be claimed by eligible employers for certain wages paid in 2018 and 2019 to qualifying employees during family and medical leave, pursuant to a written policy and subject to certain maximums and other limitations. The Internal Revenue Service (IRS) recently released a set of Q&As in Notice 2018-71 that employers will find helpful in evaluating whether or not to claim the tax credit. This article summarizes some of the notable guidance provided.

### GUIDANCE

The Notice provides much needed guidance on a number of issues related to how the requirements for the tax credit are satisfied. To be eligible for the tax credit, an employer must have in place a written policy that:

- (i) Provides at least two weeks of annual paid family and medical leave to all full-time “qualifying employees” and at least a proportionate (i.e., pro-rata) amount for part-time qualifying employees;
  - (ii) Requires a rate of payment that is at least 50 percent of the wages normally paid to such employee; and
  - (iii) If applicable, includes language stating that the employer will in no way interfere with employees’ rights under the leave policy.
- *Written Policy.* For 2018 (but not 2019), a written policy may be made retroactively effective to January 1, 2018 (or a later date), provided that it was adopted on or before December 31, 2018 and the employer made any retroactive leave payments by the last day of the taxable year.
  - *Family and Medical Leave.* Only leave taken for Family Medical Leave Act (FMLA) purposes (such as for births, adoptions, and family illnesses) may be eligible for the tax credit, and the leave may *only* be used for these purposes.
  - *Rate of Payment.* Leave paid by a State or local government or paid leave required by State or local law is not taken into account in determining an employer’s rate of payment eligible for the credit. Conversely, if State or local law does not require the leave to be paid (i.e., leave can be provided as paid or unpaid), then such leave could be taken into account in determining an employer’s rate of payment.
  - *Wages.* For purposes of determining the wages normally paid to an employee, “wages” refers to amounts normally paid for services performed, excluding overtime (other than regularly-scheduled overtime) and discretionary bonuses. For employees who are paid (in whole or in part) on a basis other than a salaried or hourly rate, until further guidance is issued, an employer must determine wages normally paid to the employee using rules under the Fair Labor Standards Act for determining an employee’s regular rate of pay.

- *Qualifying and Part-time Employees.* The Notice provides guidance on identifying qualifying employees and determining part-time status. For example, for purposes of determining part-time status, the Notice provides that an employer may use any reasonable means to calculate hours of service until further guidance is issued.
- *Providing Different Benefits.* Employers may design their policies to provide different benefits to different employee classifications or for different FMLA covered leaves, provided the minimum paid leave requirements are satisfied with respect to each FMLA covered leave for which the employer intends to claim the credit. For example, a policy could provide for differences in the rate of pay or duration of paid leave based on the employee's length of service.

#### HOW TO CALCULATE AND CLAIM THE CREDIT

The Notice also provides guidance on how to calculate and claim the credit. The tax credit is an amount equal to the applicable percentage of the amount of wages paid to qualifying employees during any period in which the employees are on family and medical leave (up to a maximum of 12 weeks). The “applicable

percentage” means 12.5 percent increased (but not above 25 percent) by 0.25 percentage points for each percentage point by which the rate of payment exceeds 50 percent.

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- *Capping the Credit.* As a rule, the credit with respect to any qualifying employee for any taxable year cannot exceed an amount equal to the product of the employee's normal hourly wage rate for each hour (or fraction thereof) of actual services performed for the employer and the number of hours (or fraction thereof) for which family and medical leave is taken. The Notice provides guidance on how employers can determine normal hourly wages for employees not paid at an hourly rate.
- *Wages.* For purposes of calculating the credit, “wages” refers to Federal Unemployment Tax Act (FUTA) wages (without regard to the FUTA wage limitation), excluding amounts taken into account for other business-related credits (e.g., research

credits). The Notice also specifies that wages paid by a third-party payor (e.g., a professional employer organization) are considered wages paid by the eligible employer for whom the employees provide services and not the third-party payor.

- *Claiming the Credit.* An eligible employer must file IRS Form 8994, Employer Credit for Paid Family and Medical Leave, and IRS Form 3800, General Business Credit, with its tax return to claim the credit. Generally speaking, each member of a controlled group makes a separate election to claim or not to claim the credit. The Notice points out that an employer's deduction for wages paid is reduced by the amount of the family and medical leave tax credit.

#### FUTURE GUIDANCE

The Notice states that the IRS intends to issue additional guidance in the form of proposed regulations that will incorporate the guidance provided in the Notice. 🌐

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