



Tax Provisions of the Families First Coronavirus Response Act

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The **Families First Coronavirus Response Act** (the “COVID-19 Response Act”), enacted on March 18, 2020, imposes two new coronavirus (COVID-19) related employment mandates on employers with fewer than 500 employees. (For details about these mandates, see “**COVID-19 Update for Employers: Congress Passes Emergency Employment Legislation; Governor Cooper Issues Executive Order on Unemployment Benefits**” written by the Smith Anderson Employment group.) The COVID-19 Response Act allows employers to recover the cost of complying with these mandates through refundable Social Security tax credits and provides similar income tax credits for self-employed individuals. This Alert summarizes these tax credit provisions.

Employment Mandates Summary

The COVID-19 Response Act includes two subparts that include employment mandates in portions entitled the Family and Medical Leave Expansion Act (the “FMLA Expansion Act”) and the Paid Sick Leave Act.

Paid Family Leave Act

The FMLA Expansion Act portion of the COVID-19 Response Act amends the Family Medical Leave Act (“FMLA”) to require employers with fewer than 500 employees to provide eligible employees with up to twelve weeks of protected leave if the employee is unable to work (or telework) in order to care for a minor child whose school or place of care has been closed, or whose regular childcare provider is unavailable, due to a COVID-19 public health emergency declared by a federal, state or local public health authority. The first 10 days of leave may be unpaid, but employers must provide paid leave of up to \$200 per day for the remaining ten weeks of leave (\$10,000 in the aggregate). In addition to the caps, the FMLA Expansion Act provides specific details about how this pay is to be calculated. Wages paid under this mandate are referred to as “qualified family leave wages.”

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Paid Sick Leave Act

The Paid Sick Leave Act portion of the COVID-19 Response Act also requires employers to provide eligible employees with ten days of sick pay if unable to work (including telework) for the following reasons:

- The employee is subject to a federal, state, or local quarantine or isolation order related to COVID-19;
- The employee has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;
- The employee has symptoms of COVID-19 and is seeking a medical diagnosis;
- The employee is caring for an individual subject to a government quarantine or isolation order or has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;
- The employee is caring for a son or daughter if the child's school or place of care has been closed, or the child's care provider is unavailable due to COVID-19 precautions; or
- The employee is experiencing any other substantially similar condition specified by the Department of Health and Human Services in consultation with the Secretary of the Treasury and the Secretary of Labor.

In all these circumstances, the employer is required to provide paid sick leave of up to \$200 per day (\$2,000 in the aggregate), except where the employee is directly subject to quarantine or isolation restrictions (the first three bullet points above), in which case the required sick leave pay is capped at \$511 per day (\$5110 in the aggregate). In addition to the caps, the Paid Sick Leave Act provides specific details on how this pay is to be calculated. Wages paid under this mandate are referred to as "qualified sick leave wages."

Social Security Tax Credits

The COVID-19 Response Act permits employers making payments of qualified sick leave wages or qualified family leave wages to claim credits equal to 100% of such payments against the employer's 6.2% old-age, survivors, and disability insurance (i.e., Social Security) tax imposed under section 3111(a) of the Code.

An IRS News Release issued on March 20th states that the credits are designed to "immediately and fully reimburse [employers], dollar-for-dollar," for the cost of the sick leave and family leave mandates by allowing businesses to "retain and access funds they would otherwise have to pay to the IRS."

Increase in Credits for Medicare Tax Payments

Qualified sick leave and family leave wages are treated as wages for purposes of calculating the 1.45% hospital insurance (i.e., Medicare) tax imposed on employers and employees. However, the employer's Social Security tax credit is increased by the Medicare tax the employer pays on any such wages for which a Social Security tax credit is allowed.

Increase in Credits for Health Plan Costs

The credits for qualified sick and family leave wages are increased by any amounts the employer pays to provide or maintain a qualified group health plan that are allocable to the creditable wages. Unless the Secretary of the Treasury provides different rules, the allocation of health plan costs may be made pro rata among covered employees and, with respect to individual employees, pro rata among periods of coverage relative to the periods of required sick leave or family medical leave to which wages relate.

Credit Limitations and Refund

The credits for qualified sick and family leave wages with respect to any employee are subject to caps depending on the employee's situation. The credit for qualified sick leave wages paid to an employee under the Paid Sick Leave Act due to the employee being subject to quarantine or isolation restrictions, the employee being advised to self-quarantine or the employee seeking a diagnosis of COVID-19 symptoms may not exceed the maximum of \$511 per day for an aggregate of up to 10 days for all calendar quarters, or \$5,110 in total for that employee. Qualified sick leave wages paid to an employee under the Paid Sick Leave Act due to any of the other allowed reasons may not exceed \$200 per day for an aggregate of up to 10 days for all calendar quarters, for a total of \$2,000 for that employee. Qualified family leave wages paid to an employee under the FMLA Expansion Act may not exceed \$200 per day for an aggregate of 50 days for all calendar quarters, for a total of \$10,000 for that employee.

Each of the qualified sick and family leave credits for any quarter cannot exceed the total employer Social Security tax for the quarter on the wages of all of the employer's employees, reduced by the credit allowed against the tax for employing veterans and that allowed against the tax for small business research and development expenditures. Any excess credit is refundable.

Other Consequences

Qualified sick and family leave wages an employer is required to pay are not treated as wages for purposes of the employer's share of Social Security taxes. The Technical Explanation of the COVID-19 Response Act prepared by the staff of Congress's Joint Committee on Taxation states that no Social Security taxes are required to be collected on such amounts from employers or employees.

An employer's gross income for the year must be increased by the amount of the qualified sick and family leave wage credits claimed for all quarters ending in such year. Thus, for example, an employer claiming a \$5,110 qualified sick leave credit would increase its gross income by \$5,110 before claiming a corresponding wage deduction of the same amount. This prevents the employer from getting the benefit of both a deduction and a credit for the same qualified sick leave wage payment.

The employer's income tax deduction for Social Security tax payments is not reduced by claiming the qualified sick leave and qualified family leave wage credits.

An employer may elect not to claim either or both of these credits.

Regulatory Authority

The Secretary is given broad authority to issue regulations or other guidance to carry out the purpose of the credit provisions. Importantly, this authority is to include guidance minimizing compliance burdens and waiving penalties for failure to deposit payroll taxes in anticipation of the enactment of the credit.

Income Tax Credits for the Self Employed

The COVID-19 Response Act provides refundable income tax credits for self-employed individuals who would be entitled to receive paid sick or family leave under the COVID-19 Response Act if such individuals were employees of employers subject to the Act.

Self-Employed Qualified Sick Leave Credit

The amount of the self-employed qualified sick leave credit is calculated by multiplying the number of days (not to exceed 10) during the taxable year that the individual would have been entitled to paid sick leave under the COVID-19 Response Act if the individual had been an employee by the lesser of two amounts: (a) \$200 (or \$511 for an individual subject to direct quarantine or isolation restrictions); or (b) 67% (or 100% for an individual subject to

direct quarantine or isolation restrictions) of the average daily self-employment income of the individual for the taxable year.

Self-Employed Qualified Family Leave Credit

Similarly, the amount of the self-employed qualified family leave credit is calculated by multiplying the number of days (not to exceed 50) during the taxable year that the self-employed individual would have been entitled to paid family leave under the COVID-19 Response Act multiplied by the lesser of two amounts: (a) \$200 or (b) 67% of the average daily self-employment income of the individual for the taxable year.

Average Daily Self-employment Income

For purposes of both of these credits, an individual's average daily self-employment income is that person's net earnings from self-employment for the taxable year divided by 260.

Self-Employed Individuals Also Receiving Wages

If a self-employed individual also receives qualified sick leave wages from an employer, the individual must reduce the self-employed qualified sick leave credit so that the sum of the self-employed qualified sick leave credit and the qualified sick leave wages received does not exceed \$2,000 (or \$5,110 in the case of an individual subject to direct quarantine or isolation restrictions).

Similarly, if a self-employed individual also receives qualified family leave wages from an employer, the individual must reduce the self-employed qualified family leave credit so that the sum of the self-employed qualified family leave credit and the qualified family leave wages received does not exceed \$10,000.

For example, assume that an individual's self-employed qualified sick leave credit is \$1,500, but that person also works for a covered employer and receives qualified sick leave wages of \$1,000 to care for his or her son or daughter while school was closed due to COVID-19. The individual's self-employed qualified sick leave credit would be reduced to \$1,000, so that the sum of the self-employed qualified sick leave credit claimed and the qualified sick leave wages received do not exceed \$2,000.

Mechanics

The March 20 IRS News Release states that the credits may be applied against the employer's entire payroll tax liability reported on Form 941, including withheld federal income taxes and the employer and withheld employee share of Social Security and Medicare taxes for all employees. According to the release, the employer would deduct the amount of the credit from the payroll tax deposit that would otherwise be due on the next regular deposit date.

Where a refund is due, the News Release states that it may be claimed through a streamlined form expected to be issued the week of March 23 and that the refund should be issued in two weeks or less.

Self-employed individuals will claim their credits on their income tax return, but the News Release states that they will be able to use the credits to reduce estimated tax payments.

Conclusion

Smith Anderson will update this Alert as additional guidance is issued by the Treasury Department or the Internal Revenue Service or if additional legislation (such as the proposed Coronavirus Aid, Relief and Economic Security Act now pending before Congress) is enacted. In the meantime, please contact a member of Smith Anderson's Tax Group if you have questions about the application of the tax provisions of the COVID-19 Response Act. Many more details about the employment mandates are also described in the Smith Anderson update: **"COVID-19 Update for Employers: Congress Passes Emergency Employment Legislation; Governor Cooper Issues Executive Order**

on **Unemployment Benefits**” written by the Smith Anderson Employment group.

Smith Anderson has developed the **Coronavirus Business Resource Center** as a tool to keep our clients and the broader business community informed on key issues that may affect their operations during these challenging times. We encourage you to check back frequently for updates and to reach out to a Smith Anderson lawyer with questions.