KPMG

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IRS guidance (updated FAQs), tax credits for small and midsize employers providing paid leave (COVID-19)

The IRS today updated a set of "frequently asked questions" (FAQs) regarding the extended and expanded tax credits for qualified paid sick and qualified family leave wages provided employees by small and midsize employers—relief measures provided in response to the coronavirus (COVID-19) pandemic.

As the **FAQs (January 28, 2021)** explain, provisions included in the "COVID-related Tax Relief Act of 2020" (enacted December 27, 2020) amended and extended tax credits—and the availability of advance payments of tax credits—for paid sick and family leave originally provided under the "Families First Coronavirus Response Act" (FFRCA). These measures provide small and midsize employers refundable tax credits that reimburse them, dollar-for-dollar, for the cost of providing paid sick and family leave wages to their employees for leave related to COVID-19.

This relief is available for businesses (referred to in the FAQs as "Eligible Employers") with fewer than 500 employees and that provide employees with paid sick and family and medical leave for reasons related to COVID-19, either for the employee's own health needs or to care for family members.

- Workers may receive up to 80 hours of paid sick leave for their own health needs or to care for others and up to an additional 10 weeks of paid family leave to care for a child whose school or place of care is closed or child care provider is closed or unavailable due to COVID-19 precautions.
- The relief covers the costs of this paid leave by providing small businesses with refundable tax credits.
- Certain self-employed individuals in similar circumstances are entitled to similar credits.

The IRS today also updated a set of **FAQs** concerning basic tax credits.

Text of the FAQs is provided below (hyperlinks have been deactivated):

Overview of COVID-19-Related Tax Credits for Small and Midsize Businesses (Updated January 28, 2021)

Under the FFCRA, employers provide paid leave through two separate provisions: (1) the Emergency Paid Sick Leave Act (EPSLA), which entitles workers to up to 80 hours of paid sick time when they are unable to work for certain reasons related to COVID-19, and (2) the Emergency Family and Medical Leave Expansion Act (Expanded FMLA), which entitles workers to certain paid family and medical leave. The FFCRA provides that Eligible Employers providing leave under the EPSLA and the Expanded FMLA are entitled to fully refundable tax credits to cover the cost of the leave paid for these periods of time during which employees are unable to work (which for purposes of these rules, includes telework). Certain self-employed persons in similar circumstances are entitled to similar credits.

The EPSLA and Expanded FMLA requires certain government employers and private employers with fewer than 500 employees to provide paid sick and family leave, respectively, to employees unable to work or telework for periods after March 31, 2020, and before January 1, 2021. The COVID-related Tax Relief Act of 2020 amended the FFCRA to extend the period for which Eligible Employers may provide paid sick and family leave to employees after December 31, 2020 and claim tax credits. Specifically, Eligible Employers that voluntarily provide paid sick or family leave to employees that otherwise would have met the requirements of the EPSLA or Expanded FMLA may claim the tax credits for providing the paid leave through March 31, 2021. However, the COVID-related Tax Relief Act of 2020 did not amend the EPSLA and Expanded FMLA, and the requirement that employers provide leave expired on December 31, 2020.

Note: *Although EPSLA and Expanded FMLA were not amended by the COVID-related Tax Relief Act of 2020, because the FFCRA tax credits are available for paid leave an Eligible Employer voluntarily provides between January 1, 2021 and March 31, 2021, only to the extent that leave would have satisfied the requirements of the EPSLA and Expanded FMLA, for convenience and ease of reference, these FAQs describe the paid leave provided during this period in 2021 as provided under the EPSLA and Expanded FMLA.*

Eligible Employers are entitled to refundable tax credits for qualified sick leave wages and qualified family leave wages (collectively "qualified leave wages"), under sections 7001 and 7003 of the FFCRA respectively. These tax credits are increased by the qualified health plan expenses allocable to, and the Eligible Employer's share of Medicare tax on, the qualified leave wages. Eligible Employers are businesses and tax-exempt organizations with fewer than 500 employees that provide paid sick leave under the EPSLA and paid family leave under the Expanded FMLA (note that although government employers may provide paid leave under the EPSLA or Expanded FMLA, those government employers are not entitled to tax credits for this leave).

Under sections 7002 and 7004 of the FFCRA, self-employed individuals are entitled to equivalent credits based on similar circumstances in which the individual is unable to work.

The refundable tax credits apply to qualified sick leave wages and qualified family leave wages paid for certain periods when an employee is unable to work, as described below, during the period beginning April 1, 2020, and ending March 31, 2021, pursuant to amendments to the provisions of the FFCRA made by the COVID-related Tax Relief Act of 2020. The same period is used to determine credits for qualified sick leave equivalent amounts and qualified family leave equivalent amounts for certain self-employed individuals.

The following section provides an overview of FFCRA's refundable tax credit provisions, and the FAQs that follow provide more detailed information regarding the requirements, limitations, and application of the paid leave credits. The Wage and Hour Division of the Department of Labor (DOL) administers the EPSLA and the Expanded FMLA and has posted FAQs and relevant *information about the paid leave requirements at the Department of Labor's Families First Coronavirus Response Act: Questions and Answers.*

Overview of Paid Sick Leave Refundable Credit (Updated January 28, 2021)

Under the EPSLA, Eligible Employers provide employees with paid sick leave if the employee is unable to work (including telework) due to any of the following:

1. *the employee is under a Federal, State, or local quarantine or isolation order related to COVID-19;*
2. *the employee has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;*
3. *the employee is experiencing symptoms of COVID-19 and seeking a medical diagnosis;*
4. *the employee is caring for an individual who is subject to a Federal, State, or local quarantine or isolation order related to COVID-19, or has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;*
5. *the employee is caring for the child of such employee if the school or place of care of the child has been closed, or the child care provider of such child is unavailable, due to COVID–19 precautions;*
6. *the employee is experiencing any other substantially similar condition specified by the U.S. Department of Health and Human Services.*

An employee who is unable to work or telework due to reasons related to COVID-19 described in (1), (2) or (3) above may receive paid sick leave for up to two weeks (up to 80 hours) at the employee's regular rate of pay, or, if higher, the Federal minimum wage or any applicable State or local minimum wage, up to $511 per day and $5,110 in the aggregate.

An employee who is unable to work or telework due to reasons related to COVID-19 described in (4), (5) or (6) above may receive paid sick leave for up to two weeks (up to 80 hours) at 2/3 the employee's regular rate of pay or, if higher, the Federal minimum wage or any applicable State or local minimum wage, up to $200 per day and $2,000 in the aggregate.

The Eligible Employer is entitled to a fully refundable tax credit equal to the required paid sick leave. This tax credit also includes the Eligible Employer's share of Medicare tax imposed on those wages and its allocable cost of maintaining health insurance coverage for the employee during the sick leave period (qualified health plan expenses). The Eligible Employer is not subject to the employer's share of social security tax imposed on those wages.

Overview of Paid Family Leave Refundable Credit (Updated January 28, 2021)

In addition to the paid sick leave credit, under the Expanded FMLA, an employee who is unable to work or telework because of a need to care for a child whose school or place of care is closed or whose child care provider is unavailable due to reasons related to COVID-19, as described in (5) above, may receive paid family and medical leave equal to two-thirds of the employee's regular pay, up to $200 per day and $10,000 in the aggregate. Up to ten weeks of qualifying leave can be counted towards the family leave credit.

The Eligible Employer is entitled to a fully refundable tax credit equal to the paid family and medical leave (qualified family leave wages). This tax credit also includes the Eligible Employer's share of Medicare tax imposed on those wages and its cost of maintaining health insurance coverage for the employee during the family leave period (qualified health plan expenses). The

Eligible Employer is not subject to the employer's share of social security tax imposed on those wages.

Payment of the Sick and Family Leave Credit (Updated January 28, 2021)

Eligible Employers are entitled to receive a credit in the full amount of the qualified sick leave wages and qualified family leave wages, plus allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax, paid for leave during the period beginning April 1, 2020, and ending March 31, 2021. The credit is allowed against the taxes imposed on employers by section 3111(a) of the Internal Revenue Code (the "Code") (the Old-Age, Survivors, and Disability Insurance tax (social security tax)) and so much of the taxes imposed on employers under section 3221(a) of the Code as are attributable to the rate in effect under section 3111(a) of the Code (the Railroad Retirement Tax Act Tier 1 rate (employer's share of social security tax)) on all wages and compensation, respectively, paid to all employees. If the amount of the credit exceeds the Eligible Employer's share of these federal employment taxes, then the excess is treated as an overpayment and refunded to the employer under sections 6402(a) or 6413(b) of the Code. The qualified sick leave wages and qualified family leave wages are not subject to the taxes imposed on employers by sections 3111(a) and, for railroad employers, the Railroad Retirement Tax Act Tier 1 rate attributable to the Eligible Employer's share of social security tax. Further, employers are entitled to an additional credit for the taxes on employers imposed by section 3111(b) of the Code and railroad employers are entitled to an additional credit for the taxes on employers imposed by section 3221(a) of the Code as are attributable to the rate in effect under section 3111(b) of the Code (Hospital Insurance (Medicare tax)) on such wages or compensation.

Note: *Section 288(e) of the COVID-related Tax Relief Act of 2020 modified the provisions of the FFCRA to clarify that the qualified leave wages paid by Eligible Employers subject to the Railroad Retirement Tax Act are excluded from the social security tax imposed on employers, but those Eligible Employers may increase the sick and family leave credits they claim by the Medicare tax imposed on qualified sick leave wages or qualified family leave wages.*

Eligible Employers that pay qualified leave wages may retain an amount of all federal employment taxes equal to the amount of the qualified leave wages paid, plus the allocable qualified health plan expenses and the amount of the Eligible Employer's share of Medicare tax imposed on those wages, rather than depositing them with the IRS. The federal employment taxes that are available for retention by Eligible Employers include federal income taxes withheld from employees, the employees' share of social security and Medicare taxes, and the Eligible Employer's share of social security and Medicare taxes with respect to all employees. Employers may also defer the deposit and payment of the employer's share of social security tax for amounts required to be deposited and paid from March 27, 2020 through December 31, 2020 (as well as deposits and payments due after January 1, 2021, for wages paid during the deferral period). Deferral of the deposit and payment of the employer's share of social security tax may be taken into account prior to retaining deposits in anticipation of the credit. In addition, employers may opt to defer withholding and payment of the employee's share of social security tax under Notice 2020-65 on certain wages paid between September 1, 2020 through December 31, 2020. (See Notice 2021-11, released on irs.gov on January 19, 2021, modifying Notice 2020-65 to reflect extended due dates for withholding and payment of the employee's share of social security taxes deferred).

If the federal employment taxes yet to be deposited are not sufficient to cover the Eligible Employer's cost of qualified leave wages, plus the allocable qualified health plan expenses and the amount of the Eligible Employer's share of Medicare tax imposed on those wages, the employer may file a request for an advance payment from the IRS using Form 7200, Advance Payment of Employer Credits Due to COVID-19

Eligible Employers claiming the credits for qualified leave wages, plus allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax imposed on those wages, must retain records and documentation related to and supporting each employee's leave to substantiate the claim for the credits, as well retaining the Forms 941 and 7200 and any other applicable filings made to the IRS requesting the credit.

For more detail on the refundable tax credits and the procedures to receive payment of the advance credit, see "How to Claim the Credits."