Apr 01, 2020

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Coronavirus Response Team
Tax Law Defined™ Blog

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Your Business, Taxes and the Families First Coronavirus Response Act

On March 18, 2020, the president signed the Families First Coronavirus Response Act (H.R. 6201, the "Act") into law. The Act goes into effect on April 1, 2020. The Act addresses some of the consequences of the coronavirus pandemic in the United States, including the closing or significant limitations on operations of many businesses, by providing for paid sick leave and imposing additional obligations on employers under the Family Medical Leave Act ("FMLA") for employers with fewer than 500 employees.

Emergency and family medical leave expansion and paid sick leave are discussed in detail in Frost Brown Todd's *Employer Update: Amended "Families First Coronavirus Response Act" Signed into Law*. Less discussed by practitioners are the tax benefits provided to employers in the Act to soften the economic impact of these new employer obligations. This update summarizes the tax provisions in the Act and also gives a general summary of state unemployment issues employers should consider at this time.

Tax Credits in the Act

The Act provides refundable tax credits for employers who are required to provide paid sick leave and emergency paid family and medical leave under the Act. The credits may be used to offset an employer's Social Security and Medicare portions of payroll tax (7.65 percent of wages paid) for each quarter. Employers may offset quarterly payroll taxes by 100 percent of the amount of qualified paid sick leave and qualified emergency paid family and medical leave actually paid to employees, subject to certain limitations discussed below. These credits are not available for amounts paid to employees who take sick, family or medical leave that is unrelated to the coronavirus outbreak. Additionally, no credit is available under the Act for wages paid to employees who take vacation or other paid-time-off.

Tax Credit for Paid Sick Leave

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Under the Act, employers are required to provide paid sick leave for a period of 80 hours for full-time employees and for the average number of hours worked in a two-week period for part-time employees. The Act imposes a limitation on the aggregate number of days per employee that can be taken into account for any quarter when calculating the sick leave credit. The maximum number of days for the second quarter of 2020 will be 10 days. For later quarters, the aggregate number of days that can be considered per quarter with respect to an individual may not exceed the excess (if any) of 10 over the aggregate number of days so taken into account for all preceding calendar quarters.

The amount of paid sick leave credit is determined based on the employees' reason for leave related to coronavirus. For each employee receiving paid sick leave because:

- the employee is subject to a government quarantine/isolation order related to coronavirus;
- the employee has been advised by a health care provider to quarantine for coronavirus concerns; or
- the employee is experiencing symptoms of coronavirus and seeking a medical diagnosis or care;

the employer receives a tax credit for that portion of wages that do not exceed $511 per employee. The sick leave credit will be increased by the amount of the employer's qualified health plan expenses (limited to the amount excluded from employee wages) that are properly allocable to the qualified sick leave wages. Therefore, if sick leave is based on the above reasons, an employer's maximum qualified sick leave credit available per employee for the second quarter of 2020 is $5,110, plus any qualified health plan expenses allocable to the sick leave wages.

If an employee is provided sick leave because:

- the employee is caring for an individual who is subject to quarantine;
- the employee is caring for the employee's child (under 18) if the school or place of care of the child has been closed, or the childcare provider of the child is unavailable due to COVID-19

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precautions; or

- the employee is experiencing any other substantially similar condition specified by the Secretary of Health and Human Services;

the employer receives a tax credit for that portion of wages that do not exceed $200 per employee. Therefore, if sick leave is based on the above reasons, an employer's maximum qualified sick leave credit available per employee for the second quarter of 2020 is $2,000, plus any qualified health plan expenses allocable to the sick leave wages.

If the amount of the qualified sick leave credit exceeds in an employer's payroll tax liability for Social Security and Medicare for the quarter, 7.65 percent of the wages paid with respect to the employment of all employees of the employer, the excess is treated as an overpayment that will be refunded to the employer.

Tax Credit for Family and Medical Leave

Family and medical leave is available for up to 10 weeks after the initial two weeks of sick leave, unpaid leave or any other leave. However, family and medical leave is limited to employees unable to work because they must care for a child whose school or childcare provider is closed due to coronavirus. Like with the sick leave credit, the family and medical leave credit is based on the amount of leave actually paid to employees, subject to limitations, and will be increased by so much of the employer's qualified health plan expenses as are properly allocable to the qualified family leave wages. For employers paying family and medical leave, the tax credit is limited to $200 of qualified family leave wages per employee per day, for a total of $10,000 per employee limit. The $10,000 per employee limit is an aggregate limit and not a per-quarter limit. The family and medical leave credit is also refundable if it exceeds the amount of the Social Security and Medicare portion of the payroll tax owed by the employer.

Example

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If an employer pays $100,000 in wages to its employees during a quarter, the employer's Social Security and Medicare portion of the payroll tax is $7,650 (7.65 percent x $100,000). If the employer's $100,000 of quarterly wages included $7,000 of qualified sick or family and medical leave payments, the employer's payroll tax obligation would be reduced from $7,650 to $650 for the quarter.

Sick Leave and Family and Medical Leave Tax Credits for Self-Employed Individuals

The sick leave credit and family and medical leave credit are both available to self-employed individuals. For eligible self-employed individuals, there is a credit against such individual's taxable income for any year in an amount equal to the "qualified sick leave equivalent amount" or "qualified family leave equivalent amount", as applicable.

The "qualified sick leave equivalent amount" and "qualified family leave equivalent amount" are determined by different formulas provided in the Act. These amounts are generally the lesser of (1) the number of days of leave (subject to previously discussed limitations), multiplied by the applicable dollar limitations of either $511 or $200, or (2) a certain percentage of the individual's daily self-employment income (100 percent or 67 percent depending on the reason for leave) multiplied by the number of days of leave (subject to previously discussed limitations).

Tax Treatment of Credits and Paid Leave and Filing Requirements

Any credit taken is included in the gross income of the employer for federal income tax. Because any sick or family and medical leave payments are available as a deduction against the employer's taxable income, including the credit taken in taxable income avoids a double tax benefit to the employer. By requiring the employer to include the tax credit into income, the employer will not receive any income tax benefit from sick or family or medical leave payments. Additionally, sick leave and family and medical leave payments under the Act are not included as wages paid for calculating the family and medical leave credit under Section 45S of the Internal Revenue Code.

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The Act provides that any sick leave and family and medical leave payments will not be considered wages for Social Security and Medicare payroll tax. As such, employers will not have to pay Social Security and Medicare payroll taxes on any sick leave or family and medical leave payments.

Taxpayers will apply the credits against payroll tax deposits due in connection with filing Forms 941, 943, 944 or CT-1. On March 30, 2020, the IRS released a DRAFT of Form 7200 which, when finalized, will allow taxpayers eligible for a refund of credits in excess of the applicable payroll taxes due to request an advance payment of any refundable credits. The draft instructions to Form 7200 explain how to request advance payment of refundable credits and can be accessed here.

Summary of State Unemployment Issues.

Once an employee is taken off payroll, he or she is generally eligible to file for unemployment with the state. However, if employees remain on payroll to use any unused vacation or sick days, he or she will not be eligible to file for unemployment until the employee is removed from payroll.

An employer wishing to allow employees to receive unemployment as soon as possible may wish to pay any accrued vacation or sick days as a lump sum severance payment on a final paycheck instead of leaving them on payroll. However, if an employer wants employees to continue to receive employer-sponsored healthcare or other benefits, having the employee remain on payroll for as long as possible may be in the best interest of the employer and employee.

The maximum unemployment weekly payment and the maximum number of weeks a person may receive unemployment varies from state to state. For example, Kentucky limits payments to a maximum of $552 per week for up to 26 weeks.

Most states have provided guidance to indicate that unemployment due to coronavirus will qualify for unemployment benefits. Employers will need to review specific state guidelines to inform employees of unemployment qualifications related to coronavirus.

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Several states, including Kentucky, Ohio and Pennsylvania, have waived the one week waiting period to receive unemployment benefits, allowing employees to receive benefits immediately.

Although additional guidance is needed, it is unlikely that the Act will apply retroactively with respect to employees who were laid off prior to the Act taking effect. As such, any employees receiving unemployment prior to the Act taking effect are unlikely to be eligible for the Act's paid leave provisions.

Generally, the number of unemployment claims increase an employer's experience rating and increase the employer's unemployment insurance payments. In other words, states assign higher state unemployment taxes to employers responsible for more layoffs. In prior disasters, states have ruled that unemployment insurance claims relating to disasters do not count against employers' experience ratings. Some states have already released similar announcements for coronavirus related unemployment insurance claims, and it is likely other states will follow, however, employers should consider the possibility of an increased experience rating when deciding to layoff employees.

We continue to follow these developments closely and will update accordingly, as both the federal and state governments continue to decipher how best to aid taxpayers during this difficult time. For more information as to how the spread of COVID-19 creates tax implications, see Tax Law Defined and Frost Brown Todd's Coronavirus Resource Page.

To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Response Team. Our attorneys are on hand to answer your questions and provide guidance on how to proactively prepare for and manage any coronavirus-related threats to your business operations and workforce.

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