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## Payroll Tax Credit for COVID-19 Sick and Family Leave

Beginning in April 2020, employers were entitled to payroll tax credits for paid leave required in response to the Coronavirus Disease 2019 (COVID-19) pandemic. For employers choosing to continue providing eligible paid leave, these tax credits have been extended through March 2021. The paid leave mandate, however, expired at the end of 2020. This In Focus provides an overview of the tax credits for paid leave initially provided in the Families First Coronavirus Response Act (FFCRA; P.L. 116-127) and extended in the COVID-related Tax Relief Act of 2020, enacted as Division N, Title II, Subtitle B of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

### Payroll Tax Credit for Paid Sick and Family Leave in FFCRA (P.L. 116-127)

FFCRA included an employer payroll tax credit for the paid sick and family leave required as part of FFCRA. This tax credit was intended to cover the cost to businesses of providing paid leave to address the COVID-19 pandemic.

### Leave Requirement

The Emergency Paid Sick Leave Act (Division E of P.L. 116-127) generally required private employers with fewer than 500 employees, and all government employers, to provide employees with two workweeks of paid sick leave for certain COVID-19-related leave purposes. The Emergency Family and Medical Leave Expansion Act (Division C of P.L. 116-127) generally provided employees of private employers with fewer than 500 employees, state and local government employees, and some federal employees expanded job-protected Family and Medical Leave Act (FMLA) leave for certain COVID-19-related caregiving responsibilities. Workers using the paid sick leave entitlement for their own needs were to be compensated at their regular rates of pay (subject to a per-day maximum), whereas leave used for caregiving was partially compensated (also subject to a per-day maximum). Employers were not required to compensate workers for the first two weeks of expanded FMLA; but after this period the leave was to be partially compensated by employers. For both sick and family leave, the law included provisions allowing employers to exclude health care providers and emergency responders from leave requirements, and allowing certain small businesses an exemption from providing leave for certain caregiving purposes.

### Employer Payroll Taxes and Paid Leave Tax Credits

The employer payroll tax credit is computed using qualifying wages paid, and claimed against the employer's share of the Social Security or railroad retirement payroll tax in each calendar quarter. Social Security payroll taxes are 12.4% of wages, with 6.2% paid by employers and 6.2% paid by employees (self-employed individuals pay the

full 12.4% amount). The Social Security payroll tax applies to workers' earnings up to an annual limit: \$137,700 in 2020 (\$142,800 in 2021). Similar taxes are withheld for railroad employees.

Employers typically deposit payroll taxes with the Internal Revenue Service (IRS) biweekly or monthly, and report employment taxes paid on quarterly federal tax returns filed within 30 days of the end of the calendar quarter. Employment payroll taxes generally are paid by all types of employers: businesses, nonprofits, and government employers.

Employers claim tax credits for FFCRA paid leave on employment tax returns, which are generally filed quarterly (certain small employers may file annually). Employers can reduce payroll tax deposits in anticipation of receiving paid leave tax credits. Employers can also request an advance of tax credit amounts. The tax credit is refundable, meaning that if the amount of tax credits an employer claims exceeds payroll tax liability, the excess is received as a payment from the Treasury. Employers claiming the credit are required to include the amount claimed in gross income, for income tax purposes, offsetting the reduction in gross income from deducting wages paid (preventing a double benefit). Additionally, employers cannot claim this credit for any wages taken into account for the purposes of calculating the Section 45S employer tax credit for paid family and medical leave. Employers may also elect not to have the credit apply. The credit does not apply to government employers.

The Social Security trust funds will not be affected by the tax credit. A general fund transfer to the trust funds offsets any reduction in trust funds revenues from the tax credit.

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Employer payroll tax credits offset the cost of providing COVID-19-related paid leave. Employers were required to provide COVID-19-related paid leave from April through December 2020. In 2021, tax credits may be available for employers choosing to provide paid leave.

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### Qualifying Sick Leave Wages

Employers can claim a tax credit for 100% of the amount required to be paid in sick leave wages. Sick leave wages must be paid for up to 80 hours (two workweeks) for a full-time employee (prorated for part-time employees). The maximum amount that must be paid to workers using FFCRA sick leave depends on the purpose for which the sick leave is taken.

Sick leave wages cannot exceed \$511 per day for employees if they are taking leave because (1) the employee is subject to 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 COVID-19; or (3) the employee is experiencing symptoms of COVID-19 and is seeking a medical diagnosis.

Sick leave wages cannot exceed \$200 per day for employees if they are taking leave because (A) the employee is caring for an individual (with whom the employee has a close personal relationship) who is experiencing a situation described in number (1) or (2) above; (B) the employee is caring for their own minor child whose school, place of care, or caregiver is closed or unavailable due to COVID-19; or (C) the employee is experiencing any other “substantially similar condition” as specified by the Secretary of Health and Human Services.

The tax credit amounts for paid sick leave can be increased by the amount employers pay for an employee’s health care plan while they are on leave.

### ***Qualifying Family and Medical Leave Wages***

The employer tax credit for paid family leave is for employees who take leave because they must care for their own minor child whose school or place of care was closed due to COVID-19.

For this component of the credit, the paid leave period begins after an individual has already taken 10 days of leave for the family leave purpose described above. These 10 days of leave may consist of unpaid leave, or an employee may elect to use paid vacation, personal, or another form of paid leave (including the FFCRA paid sick leave). After this 10-day period, employees will receive a benefit from their employers that is at least two-thirds of the employee’s usual pay, but not more than \$200 per day. The tax credit for family leave wages is limited to \$200 per day, and \$10,000 total per employee. The tax credit amounts for paid family leave can be increased by the amount employers pay for an employee’s health care plan while they are on leave.

### ***Income Tax Credit for Self-Employed Individuals***

Self-employed individuals, including gig workers, are eligible for income tax credits similar to those described above. If individuals are unable to perform services in their trade or business for the sick leave purposes described above, the individual may qualify for an income tax credit equal to 100% of average daily self-employment income. Like the employer credits, this credit is limited to \$511 per day for certain qualifying sick leave purposes, and \$200 for other sick and qualified family leave purposes. The sick leave credit is limited to a maximum of 10 days (i.e., a maximum of \$5,110 per worker). The family leave credit is limited to 50 days (i.e., a maximum of \$10,000 per worker). For self-employed individuals, the income tax credit is refundable (meaning that if the tax credit amount exceeds the individual’s income tax liability, the excess is received as a refund, or payment, from the Treasury).

## **Extension of Paid Leave Tax Credits in P.L. 116-260**

The COVID-related Tax Relief Act of 2020 extended the payroll tax credits for paid leave through March 31, 2021. The credits apply *as if* the corresponding employer mandates were also extended. The payroll tax credits for paid leave are thus available for employers voluntarily providing qualifying paid leave through March 31, 2021.

The legislation does not modify the overall caps on the paid leave amounts for which tax credits can be claimed. Thus, tax credits are limited to a total of 80 hours of paid COVID-19-related sick leave and 10 weeks of paid family leave for certain COVID-related childcare purposes from April 1, 2020, to March 31, 2021.

### **Policy Considerations**

The Joint Committee on Taxation (JCT) estimated that the paid leave tax credits in FFCRA would reduce tax revenue by \$104.9 billion, the combined total for fiscal years 2020 and 2021. Extending the tax credits through March 31, 2021, was estimated to reduce federal tax revenue by an additional \$1.6 billion, with the reduction taking place in fiscal years 2021 and 2022.

An October 2020 study found that enhanced access to paid leave reduced the spread of COVID-19 (see Stefan Pichler, Katherine Wen, and Nicolas R. Ziebarth, “COVID-19 Emergency Sick Leave Has Helped Flatten the Curve in the United States,” in *Health Affairs*, at <https://www.healthaffairs.org/doi/full/10.1377/hlthaff.2020.00863>). This research is consistent with broader evidence that access to paid sick leave can reduce transmission of contagious viruses.

The paid leave mandate in FFCRA was not comprehensive. The legislation expanded access to paid sick and family leave for employees at many small and mid-sized businesses. Employees of large businesses and certain worker groups, however, did not have guaranteed access to paid sick or family leave under FFCRA.

Similarly, the tax credits provided in FFCRA were not available to all employers required to provide leave. State and local government employers, including school districts and public colleges and universities, were required to provide leave but not allowed tax credits to offset the cost of complying with the FFCRA leave mandate.

### **Additional Resources**

- Internal Revenue Service, “COVID-19-Related Tax Credits for Required Paid Leave Provided by Small and Midsize Businesses FAQs,” available at <https://www.irs.gov/newsroom/covid-19-related-tax-credits-for-required-paid-leave-provided-by-small-and-midsize-businesses-faqs>.
- CRS In Focus IF11487, *The Families First Coronavirus Response Act Leave Provisions*, by Sarah A. Donovan and Jon O. Shimabukuro.

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