Tax Treatment of Paid Family Leave Benefits

Updated March 28, 2019

State	Own Disability[1]			Family Care[2]		
	State Tax	**Federal Tax**	**Social Security/ Medicare/ FICA**	**State Tax**	**Federal Tax**	**Social Security/ Medicare/ FICA**
CA	No, except when considered a substitute for UI[3]	No, except when considered a substitute for UI	No	No (Contributions post-tax)	Yes (Contributions deductible)	No
NJ	Employer Portion: Yes/ Employee Portion: No	Employer Portion: Yes/ Employee Portion: No	FICA on employer portion, not on employee portion	No (Contributions post-tax)	Yes (Contributions deductible)	No
RI	No	No	No	Yes (Contributions deductible)	Yes (Contributions deductible)	No
NY	Employer Portion: Yes/ Employee Portion: No	Employer Portion: Yes/ Employee Portion: No	FICA on employer portion, not on employee portion	Yes	Yes (Contributions to State plan deductible)[4]	No
H.107 (as amended by HWM)	Employer Portion: Yes/ Employee Portion: No	Employer Portion: Yes/ Employee Portion: No	FICA on employer portion, not on employee portion	Yes	Yes (Contributions deductible)	No
Unemployment	N/A	N/A	N/A	Yes	Yes	No
Workers' Comp	No	No	No	N/A	N/A	N/A

[1] Includes benefits paid in relation to the employee's own serious illness, and possibly leave related to an employee's pregnancy if it is taken because of a pregnancy related disability.
[2] Includes benefits paid in relation to leave during pregnancy, for bonding with a new child, or to care for a seriously ill relative.
[3] If an individual is receiving UI benefits, becomes unable to work due to a disability, and begins receiving CA SDI benefits, his or her SDI benefits are considered a substitution for UI benefits and are reportable for tax purposes.
[4] Contributions to a private or self-insured plan are considered non-deductible personal expenses. Rev. Rul. 81-192.

Answers to Frequently Asked Tax Questions Regarding H.107

How are benefits taxed when they are paid to an employee?

- Taxable if considered unemployment compensation.[5]
  - Benefits provided for family care and bonding are considered unemployment compensation.
- Non-taxable if considered disability-based compensation.[6]
  - Benefits paid for an employee's own disability are considered disability-based compensation.
  - However, benefits are taxable to the extent they are paid for by the employer.

How are employee contributions to the Family and Medical Leave Insurance Program treated for tax purposes?

- Likely treated as a payment of a State income tax.[7]
- Deductible as an itemized deduction on federal taxes.[8]
  - Recent federal tax changes have reduced the likelihood that an individual will itemize deductions.
- Benefits paid to non-itemizers is only taxed on amounts received in excess of the employee's contribution
  - Benefit for itemizers is taxed on all benefits (while allowing the deduction).
- Not deductible on State level because Vermont does not allow itemized deduction for State taxes.

Are the contributions for the State Program Pre-Tax or Post-Tax?

- Employee contributions to a family leave program are deductible as a state income tax. State income taxes are paid with post-tax dollars; therefore, the employee contributions are paid from post-tax dollars.

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[5] 26 U.S.C. § 85.
[6] 26 U.S.C. § 104.
[7] *See* Rev. Rul. 81-192 ("The word 'taxes' has been defined as an enforced contribution, exacted pursuant to legislative authority in the exercise of the taxing power, and imposed an collected for the purpose of raising revenue to be used for public or governmental purposes and . . . paid to a government levying the tax, to certain public benefit corporations created by that government for a public purpose, or to their agents."); IRS Memorandum 200630017, California Paid Family Leave, June 1, 2005, available at https://www.irs.gov/pub/irs-wd/0630017.pdf.
[8] *See* IRS Memorandum 200630017.

Would employee contributions affect the Homestead Property Tax income sensitivity adjustment?

- Income sensitivity starts with federal adjusted gross income and there are no applicable exclusions.[9]
- Therefore, employee contributions would likely count as income for purposes of calculating income sensitivity.

Are FICA (Social Security and Medicare) taxes due on the benefits received by an employee?

- Potentially. FICA is due on wages paid by an employer and on disability benefits financed by an employer.
- Under H.107, as recommended by the House Ways and Means Committee, Family and Medical Leave Insurance benefits could be jointly financed by employers and employees and therefore FICA contributions could be due in relation to the portion of the benefits financed by the employer.
- However, benefits provided for bonding leave or family care are not considered wages and therefore are not subject to FICA.

How would a voluntary employer contribution be treated?

- A voluntary employer contribution would likely be considered deductible to the employer as a business expense.[10]

How would an alternative insurance plan be treated?

- Employer contributions would be considered a deductible business expense.[11]
- Employee contributions would be considered a non-deductible personal expense.[12]
- Benefits received by an employee for his or her own disability would be taxable to the extent of the employer contribution.[13]
- Benefits for family care and bonding would be taxable to the employee.[14]

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[9] 32 V.S.A. § 6061(5).
[10] Because any employer contribution is voluntary, and the amount is not set by statute, it is considered a business expense and not a tax.
[11] *See* Rev. Rul. 81-193.
[12] *Id*.
[13] *See* 26 U.S.C. § 104(a)(3); Rev. Rul. 81-194.
[14] *See* 26 U.S.C. § 85; Rev. Rul. 81-194.

Would Employers be Eligible for the Federal Employer Credit for Paid Family and Medical Leave?

- No. The federal tax credit for benefits paid in relation to an employer-provided paid family leave program do not apply to "any leave which is paid by a State or local government or required by State or local law."[15]
- In addition, without further Congressional action, the tax credit is set to expire on December 31, 2019 and the benefits proposed in H.107 would not become available until July 1, 2020.

[15] 26 U.S.C. § 45s(c)(4).