

**Tax Treatment of Paid Family Leave Benefits**

Updated February 21, 2019

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

<sup>1</sup> 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.

<sup>2</sup> Contributions to a private or self-insured plan are considered non-deductible personal expenses. Rev. Rul. 81-192.

<sup>3</sup> 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.

<sup>4</sup> Includes benefits paid in relation to leave during pregnancy, for bonding with a new child, or to care for a seriously ill relative.

## **Answers to Frequently Asked Tax Questions Regarding H.107**

### **How are benefits taxed to an employee when they are paid out?**

- Taxable if considered unemployment compensation.<sup>5</sup>
  - Benefits provided for family care and bonding are considered unemployment compensation.
- Non-taxable if considered disability-based compensation.<sup>6</sup>
  - Benefits paid for an employee's own disability are considered disability-based compensation.

### **Are the Contributions for Paid Family Leave Benefits 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.

### **How are employee contributions taxed?**

- Treated as a payment of a State income tax.<sup>7</sup>
- Deductible as an itemized deduction on federal taxes.<sup>8</sup>
  - Recent federal tax changes have reduced the likelihood that an individual will itemize deductions.
- Benefit for 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.

### **Would employee contribution affect income sensitivity?**

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

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<sup>5</sup> 26 U.S.C. § 85.

<sup>6</sup> 26 U.S.C. § 104.

<sup>7</sup> See Rev. Rul. 81-191; IRS Memorandum 200630017, California Paid Family Leave, June 1, 2005, available at <https://www.irs.gov/pub/irs-wd/0630017.pdf>.

<sup>8</sup> See IRS Memorandum 200630017.

<sup>9</sup> 32 V.S.A. § 6061(5).

**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, Family and Medical Leave Insurance benefits would be jointly financed by employers and employees and therefore FICA contributions would 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 mandatory employer contribution be treated for tax purposes?**

- Most likely treated as a deductible state tax for both unemployment or disability-based compensation.<sup>10</sup>

**How would a voluntary employer contribution be taxed?**

- For disability-based compensation, a voluntary employer contribution would likely be considered deductible to the employer as a business expense, and taxable to the employee to the extent of the employer contribution.<sup>11</sup>
- For family care and bonding benefits, the payment would likely be considered deductible to the employer as a business expense, and taxable to the employee.<sup>12</sup>

**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.”<sup>13</sup>
- 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 October 1, 2021.

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<sup>10</sup> See Rev. Rul. 81-194.

<sup>11</sup> See Rev. Rul. 81-194.

<sup>12</sup> See 26 U.S.C. § 85; Rev. Rul. 81-194.

<sup>13</sup> 26 U.S.C. § 45s(c)(4).