



Recent COVID-19 Legislation Provides Payroll Tax Relief to Employers

The two Coronavirus aid and relief laws recently passed by Congress include a number of tax provisions, including several which allow employers to use payroll tax withholdings as a source of working capital to partially compensate for the cost of mandated sick leave and family leave pay, employee furloughs and business reduction. This article will outline the new payroll tax provisions in the Families First Coronavirus Response Act (FFCRA) and the Coronavirus Aid, Relief and Economic Security (CARES) Act. Each permits payroll taxes to be used for working capital in different situations. As with any legislation created in a very compressed timeframe there are lots of unanswered questions but the IRS has indicated that it intends to issue further guidance later this week.

Tax Credits for Paid Sick Leave and Paid Family and Medical Leave

Effective April 1, 2020, the Families First Coronavirus Response Act (FFCRA) requires private employers with less than 500 employees to provide employees with paid sick leave and expanded paid family and medical leave benefits under certain circumstances as a result of COVID-19. [Click here](#) for a link to our COVID-19 Resource Center for all of our latest e-Alerts, webinars and podcasts surrounding the coronavirus pandemic.

The FFCRA allows employers who make qualifying sick leave and expanded family medical leave payments to employees between April 1, 2020 and December 31, 2020 to recoup the cost of these payments from the payroll taxes that the employer is otherwise required to periodically withhold and deposit with respect to taxable wages paid to all of its employees.

In addition to there being uncertainty about the details of the process by which employers can use payroll taxes as a source of working capital, there is some uncertainty about the types of payroll taxes that can be used for this purpose. The FFCRA permits some but not all payroll taxes to be used, but on March 20th the IRS issued Release IR-2020-57 and took a more liberal approach that may not be fully supported by the law. Additional guidance will hopefully be issued this week to clarify this apparent discrepancy.

The FFCRA allows an employer to take a credit against its quarterly FICA tax obligations for the amount of sick leave and extended family and medical leave paid during that quarter. An

employer's FICA tax obligation consist of two parts, 6.2% of wages for Social Security taxes and 1.45% of wages for Medicare taxes. The FFCRA allows an employer to claim a credit for the employer's share of these FICA taxes but not for any FUTA or state taxes that the employer is required to withhold. It is unclear whether the credit is available for the employee's share of FICA taxes as well.

To illustrate what is clear under the new law, if an employer owes \$10,000 in employer FICA taxes for compensation paid to all of its employees during a fiscal quarter, and it paid \$3,000 in sick leave under FFCRA to certain employees during that quarter, the employer can take a credit for the \$3,000 of sick leave and reduce its FICA tax deposit to \$7,000. As a result, the employer would not be required to deposit the \$3,000 and could use these funds for working capital. If the employer paid \$12,000 in sick leave during the quarter, the amount of available credit (\$12,000) would exceed the employer's \$10,000 FICA tax obligation for the quarter and the employer would not be required to deposit any employer FICA taxes for the quarter. In addition, the employer would be entitled to apply for a refund of the \$2,000 excess credit. However, since payroll tax returns are not filed until 30 days after the end of the quarter, it might take another 30-60 days thereafter (or longer) to obtain a refund of the excess credit.

Release IR-2020-57 made a significant change to the taxes for which the credit is available. The Release states that an employer can claim the credit not only against the employer's share of FICA taxes due for a fiscal quarter but also against the employee share of FICA taxes and any federal income taxes withheld from wages paid to all employees during the quarter. The Release notes that the goal of the credit is to provide an employer with an immediate, dollar for dollar offset against payroll taxes and thereby free up these funds for use in the employer's business. The Release also notes that the IRS will endeavor to send refunds of excess credits to the employer as quickly as possible. The IRS commitment to prompt refunds was subsequently underscored by a provision included in the CARES Act, which authorizes advance refunding of the excess credits by means of forms and procedures to be developed by the IRS.

Release IR-2020-57 provides the following examples illustrating the operation of the credit:

Example #1: An employer paid its employees an aggregate of \$5,000 in sick leave during the quarter and is required to deposit \$8,000 in payroll taxes with respect to taxable compensation paid to all of its employees during the quarter. FFCRA permits the employer to use \$5,000 of the \$8,000 that it was going to deposit to reimburse itself for the cost of its sick leave payments. The employer would be required to deposit the remaining \$3,000 of withholdings at its next regular deposit date.

Example #2: An employer paid \$10,000 in sick leave during the quarter and was required to deposit \$8,000 in withholdings with respect to all employee wages paid during the quarter. The FFCRA allows the employer to use the entire \$8,000 of withholdings to reimburse itself for its sick leave payments. In addition, the employer can file a request for an accelerated refund for the remaining \$2,000.

Can employers rely on the Release IR-2020-57 and not only take the payroll tax credit against employer FICA taxes but also against employee FICA taxes and employee income tax withholdings? Hopefully upcoming IRS guidance provide clarification.

We also hope that guidance will provide clarification on how an employee will get credit for any withheld income taxes against which the employer claimed a credit and, as a result, presumably did not remit to the Treasury to be applied against the employee's 2020 income taxes. The FFCRA requires Congress to appropriate and remit to the Social Security Trust Fund any employer FICA taxes diverted to the employer as a payroll credit but this appropriation order does not appear to include employee FICA taxes and does not apply to employee income taxes. How will the Trust Fund and the Treasury be made whole for these taxes? If the approach described in the IRS Release is binding, at the very least employers will need to keep careful records of the underlying source of the payroll tax deposits that they claim as a credit and divert to their own use—i.e., what specific payroll taxes were involved and from which employees did they originate?

An employer typically makes payroll tax deposits on multiple occasions during the course of a fiscal quarter. Once made, it does not appear that the employer has the right to get any of these deposits back as a credit against future sick leave or extended family and medical leave payments made during the quarter—i.e., the employer can only apply the FFCRA payroll credit against future payroll taxes that it would otherwise be required to deposit during that quarter.

There are a number of other aspects of the new FFCRA payroll credit. They include the following:

- In addition to claiming a credit for qualified sick leave and extended family and medical leave paid during a quarter, an employer may claim a credit for that portion of the employer's health plan expenses that are allocable to the sick leave or family and medical leave for which the credit is allowed to the extent that these health plan expenses are excluded from the employee's income.
- The payroll credit is not available for qualified sick leave and family and medical paid under FFCRA prior to April 1st.
- Although an employer can elect to provide sick leave and family and medical leave in excess of the FFCRA limits, the employer will not be eligible for a credit for these excess payments. In addition, if an employee elects to substitute accrued vacation leave, personal leave or medical or sick leave for FFCRA paid leave, the substituted payments will not be eligible for the credit.
- The employer must include as income any amounts claimed as a credit. For example, if an employer claims a credit of \$5,510 for \$5,110 of qualified sick leave and \$400 of health plan expenses during the quarter, the employer will be required to include \$5,510 as additional income and can deduct \$5,110 of sick leave and \$400 of health plan expenses.
- Any qualified sick leave or family and medical leave taken into account for purposes of the FFCRA payroll credit is not eligible for the tax credit permitted under Code Section 45S for certain family and medical leave but any such leave in excess of the FFCRA limits

may be eligible for the 45S credit. Employers should evaluate whether claiming the 45S credit for these wages is more advantageous than claiming the FFCRA payroll credit.

- The credit for FFCRA paid sick leave is only available for 10 days of sick leave payments (up to a maximum of 80 hours). If an employee is taking FFCRA sick leave for 5 hours a day to take care of a child and is able to telework remotely from home during the other 3 hours (and is being paid regular wages for this work), the employer can only claim a payroll credit for the 5 hours of sick leave and will not be able to claim this credit after the first 10 days of sick leave have ended even if the employee is eligible for continued FFCRA sick leave in subsequent weeks because the employee has not used up the 80 hours of available sick leave pay.
- Similar benefits are provided to self-employed individuals.

CARES Act Payroll Tax Benefits

Ten days after the FFCRA was signed into law the President signed a second COVID-19 relief bill entitled the Coronavirus Aid, Relief and Economic Security (CARES) Act that included several tax incentives, including two payroll tax incentives.

The first payroll incentive rewards employers for retaining employees (even if on a reduced or furloughed basis) and allows employers to use certain payroll taxes as a source of working capital. It provides employers with a refundable payroll tax credit for 50 percent of eligible wages paid by eligible employers to certain employees. The credit is provided for the first \$10,000 in wages and other types of compensation paid after March 12, 2020 and before January 1, 2021. Health benefits paid during this period are eligible for the credit and count towards the \$10,000 cap.

The Secretary of the Treasury is granted authority to advance payments to eligible employers and to waive applicable penalties for employers who do not deposit applicable payroll taxes in anticipation of receiving the credit.

Eligible employers are defined as all private employers, including non-profits, whose operations have been fully or partially suspended as a result of a government order limiting commerce, travel or group meetings. Eligible employers also include any employers who have experienced a greater than 50% reduction in quarterly receipts, measured on a year-over-year basis. However, the credit is not available to employers receiving Small Business Interruption Loans.

Wages eligible for the credit:

- For employers whose average number of full-time employees in 2019 was more than 100 full-time employees, eligible wages consist of wages paid to employees who are furloughed or face reduced hours as a result of their employers' closure or economic hardship
- For employers whose average number of full-time employees in 2019 was 100 or less, all employee wages are eligible, regardless of whether an employee is furloughed.
- Eligible wages do not include wages taken into account for purposes of the FFCRA payroll credits for qualified paid sick leave or family and medical leave, nor for wages taken into account for the employer credit under Code Section 45S for paid family and medical leave

The second payroll incentive allows employers to defer paying the employer portion of FICA taxes due (after reduction for any payroll credits claimed under the provisions discussed above) for the period commencing on the date of enactment of the Act (March 27, 2020) and before January 1, 2021. The employer will not be required to deposit the deferred taxes and can use them as working capital for its business.

Any taxes deferred under this provision will be due in two equal installments, one on December 31, 2021, and the other on December 31, 2022. This deferral is not provided to employers that obtain SBA 7(a) loans designated for payroll.