

IRS Issues Guidance on COVID-19-Related Tax Credits Available to Employers Under the FFCRA

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On April 1, 2020, the Internal Revenue Service (“IRS”) posted on its website a series of frequently asked questions (“[FAQs](#)”) that explain the COVID-19-related tax credits available to small and midsize employers who are required to provide paid leave under the Families First Coronavirus Response Act (the “FFCRA”), which was signed into law by President Trump on March 18, 2020. This blog summarizes some of the key items addressed by the FAQs, including which employers are eligible for these credits, and the requirements and documentation necessary for claiming the credits.

Overview of COVID-19-Related Tax Credits Available to Employers Under the FFCRA

The FFCRA imposes obligations on private employers and nonprofit organizations with fewer than 500 employees^[1] to provide paid leave to employees that are unable to work for certain reasons related to COVID-19.

Paid Sick Leave. Under the Emergency Paid Sick Leave Act (the “EPSLA”), an employer is required to provide paid sick leave to an employee that is unable to work (or telework) due to the following reasons:

1. the employee is under 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 concerns related to COVID-19;
3. the employee is experiencing symptoms of COVID-19 and seeking a medical diagnosis;
4. the employee is caring for an individual who is subject to a federal, state, or local quarantine

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- or isolation order related to COVID-19, or has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;
5. the employee is caring for the child of such employee if the school or place of care of the child has been closed, or the child care provider of such child is unavailable, due to COVID-19 precautions;
 6. the employee is experiencing any other substantially similar condition specified by the U.S. Department of Health and Human Services.^[2]

An employer must pay an employee who is unable to work due to a COVID-19 circumstance described in (1), (2), or (3) above his or her full regular wage (up to \$511 per day or \$5,110 total) for sick leave of up to 10 days (up to 80 hours). The EPSLA also requires an employer to pay an employee who is unable to work due to a COVID-19 circumstance described in (4), (5), or (6) above two-thirds of his or her regular wage (up to \$200 per day or \$2,000 total) for sick leave of up to 10 days (up to 80 hours).

Regulations issued by the U.S. Department of Labor provide that, for purposes of the FFCRA, a quarantine or isolation order includes quarantine, isolation, containment, shelter-in-place, or stay-at-home orders issued by any federal, state, or local government authority, such as the stay-at-home order in effect in California or the “On PAUSE” executive order in effect in New York, that cause the employee to be unable to work even though his or her employer has work that the employee could perform but for the order.^[3] However, the Regulations provide that an employee subject to one of these orders may not take paid sick leave where the employer does not have work for the employee. This is because the employee would be unable to work even if he or she were not required to comply with the quarantine or isolation order.

Paid Family Leave. In addition to the paid sick leave under the EPSLA, an employer is also required under the Emergency Family and Medical Leave Expansion Act to pay an employee two-thirds of his or her regular wage (up to \$200 per day and \$10,000 total) for family leave of up to 10 weeks if the employee is unable to work (or telework) because of a need to care for a child whose school or place of care is closed or whose child care provider is unavailable due to COVID-19. An employer is required to provide this paid family leave only after an employee has been unable to work or telework for 80 hours for these reasons. Wages for the first 80 hours may be covered by the requirements under the EPSLA if the employee so elects.

Refundable Credit for Paid Sick and Family Leave. An employer subject to these requirements is entitled to a refundable tax credit equal to (i) the wages (“qualified leave wages”) for paid sick and family leave described above that is taken between April 1, 2020 and December 31, 2020 and (ii) the employer’s share of Medicare tax imposed on those wages and its allocable cost of maintaining health insurance coverage for the employee during the leave period (“qualified health plan expenses”), even if the payments of the wages are made after this period. The employer is not subject to the employer portion of Social Security tax imposed on those wages.^[4]

The instructions to Form 7200, *Advance Payment of Employer Credits Due to COVID-19*, provide that an employer may use the paid sick and family leave credits under the FFCRA to offset all federal employment taxes (including federal withholding tax, and the employer’s and the employee’s share of Social Security and Medicare taxes).

Comparable credits are available to self-employed individuals that take sick or family leave between April 1, 2020 and December 31, 2020 if they regularly carry on a trade or business (within the meaning of section 1402^[5]) and would be entitled to receive qualified leave wages under the FFCRA

if the individual were an employee of an employer (other than himself or herself) that is subject to the requirements of the FFCRA. A self-employed individual is eligible for a credit that covers 100% of his or her qualified sick leave equivalent amount, or 67% of the individual's qualified sick leave equivalent amount if they are taking care of a sick family member, or taking care of a child following the child's school closing. A self-employed individual's qualified sick leave equivalent amount is the number of days during the taxable year that the individual cannot perform services and is entitled to sick leave (up to 10 days), multiplied by the lesser of average daily self-employment income (or 67% of that income if they are taking care of a sick family member or child following a school closing), or \$511 per day for sick leave (or \$200 per day to care for a sick family member or child following a school closing). Self-employed individuals can receive a family leave credit for up to 50 days multiplied by the lesser of \$200 or 67% of their average self-employment income, up to a maximum of \$10,000.

Obtaining the Tax Credits under FFCRA

Claiming the Credits.

An employer reports its total qualified leave wages (and allocable qualified health plan expenses and share of Medicare tax on the qualified leave wages) for each quarter on its federal employment tax return, generally Form 941, *Employer's Quarterly Federal Tax Return*. If an employer receives an advance of the credits by submitting the Form 7200, it will be required to account for the amounts received as an advance when it files its Form 941 for the relevant quarter.

Substantiating Eligibility for the Credits.

An employer claiming the credits for qualified leave wages (and allocable qualified health plan expenses and the employer's share of Medicare taxes) must retain records and documentation related to and supporting each employee's leave to substantiate the claim for the credits. The employer must receive from its employee a written request for paid leave that includes the employee's name, the dates of leave, the specific COVID-19-related reason for the requested leave and supporting evidence, and a statement that the employee is unable to work (or telework) for that reason.

For a leave request based on self-quarantine or a quarantine or isolation order, written support should identify the healthcare professional advising or governmental entity ordering the quarantine. If the individual subject to quarantine is not the employee, written support should identify the individual and their relation to the employee. For a leave request based on a lack of child care (i.e., school closure or unavailable childcare provider), the employee should provide the name and age of any children to be cared for, the name of the school or care provider that is unavailable, and a representation that no other person will be providing care for the child during the period for which the employee is receiving family medical leave. For children over the age of 14, the employee must include a statement that special circumstances exist that require the employee to provide care, and are unable to work or telework as a result.

In addition to the employee's written support, an employer should maintain, for at least 4 years after the later date of when the tax becomes due or is paid, certain records to substantiate eligibility for this tax credit, including documentation demonstrating how the employer determined the amount of qualified leave wages paid to eligible employees, documentation demonstrating how the employer determined the amount of qualified health plan expenses that the employer allocated to wages, and

copies of any relevant IRS filings, such as Forms 941 and 7200.

Eligibility for the Tax Credits under FFCRA

Employers entitled to claim the refundable tax credits are businesses and tax-exempt organizations that have fewer than 500 employees, and are required under the FFCRA to pay qualified leave wages.

A business is considered to have fewer than 500 employees if, at the time an employee's leave is to be taken, the business employs fewer than 500 full-time and part-time employees within the United States. The U.S. Department of Labor issued guidance that provides a more detailed summary of which workers must be taken into account for purposes of this threshold.^[6] The guidance also explains when business entities should be treated as separate employers and when they should be aggregated as a single employer for purposes of determining their total number of employees. Under the guidance, subsidiaries and other entities within a controlled group (as defined in section 414(b)^[7]) may be treated as separate employers for purposes of determining whether a business has fewer than 500 employees.

Under certain circumstances, an employer with fewer than 50 employees is exempt from the requirements to provide paid sick leave or expanded family and medical leave due to school or place of care closures or child care provider unavailability for COVID-19 related reasons when doing so would jeopardize the viability of the small business as a going concern.^[8] Accordingly, an employer exempt from these obligations would not be entitled to the tax credits for qualified leave wages.

An employer that is otherwise eligible to receive the credits is entitled to the credits regardless of whether it uses a third party payer to report and pay its federal employment taxes. The third party payer is not entitled to the credits with respect to the wages it remits on the employer's behalf regardless of whether the third party is considered an "employer" for other purposes of the Internal Revenue Code.

If an employer uses a third party to file, report, and pay federal employment taxes, certain rules for claiming and reporting the credits will apply depending on the type of third party payer the employer uses.

If an employer uses a certified professional employer organization ("CPEO") or a 3504 agent (i.e., a third-party agent that performs some or all of the employer's federal employment tax withholding, tax return preparation, reporting, and tax payment responsibilities) to report its federal employment taxes on an aggregate Form 941, the CPEO or 3504 agent will report the credits on its aggregate Form 941 and Schedule R, *Allocation Schedule for Aggregate Form 941 Filers*, that it already files. The employer can submit its own Form 7200 to claim the advanced refund, but will need to provide a copy of the Form 7200 to the CPEO or 3504 agent so the CPEO or 3504 agent can properly report the credit on the Form 941.

If an employer uses a non-certified PEO to report and pay its federal employment taxes, the PEO will need to report the credits on an aggregate Form 941 and separately report the credits allocable to the employers for which it is filing Form 941 on an accompanying Schedule R. The PEO does not have to complete Schedule R with regard to employers for which it is not claiming a credit. The employer will need to provide a copy of any Form 7200 that it submitted for an advanced refund to the PEO so it can properly report the credit on the Form 941.

Interaction of the Tax Credits under the FFCRA and Other Tax Credits and COVID-19 Relief

The credits are not available for an employer receiving a credit for paid family and medical leave under the 2017 Tax Cut and Jobs Act (the “TCJA”).^[9] An employer may receive both the tax credits for qualified leave wages under the FFCRA and the employee retention credit under the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”), but not for the same wage payments.

Companies receiving small business interruption loans under the Small Business Administration’s paycheck protection program are eligible for the tax credits under the FFCRA.

Employers: Taxation and Deductibility of Tax Credits under the FFCRA

Generally, an employer’s payments of qualified leave wages (and any allocable qualified health plan expenses and the employer’s share of the Medicare tax on the qualified wages) are deductible by the employer as ordinary and necessary business expenses in the taxable year that these wages are paid or incurred. Accordingly, an employer may deduct as a business expense the amounts paid to an employee for qualified leave wages (and any allocable qualified health plan expenses and the employer’s share of Medicare tax on the qualified leave wages) for which the employer expects to claim the tax credits under the FFCRA, if the employer is otherwise eligible to take the deduction.

An employer’s payment of payroll taxes is generally deductible by the employer as an ordinary and necessary business expense in the taxable year that these taxes are paid or incurred, and the amount deductible is generally reduced by credits allowed. Although the tax credits under the FFCRA are allowed against the employer’s portion of the Social Security tax, the credits are treated as additional taxable income to the employer. The tax credits under the FFCRA are allowed against federal income tax withholding, the employer’s and employee’s share of Social Security and Medicare taxes (but cannot offset the employer’s Federal Unemployment Tax Act (“FUTA”) liability). The credits are treated as additional taxable income to the employer.

Employees: Taxability of Qualified Leave Wages

Qualified sick and family leave wages are treated as taxable wages subject to withholding of federal income tax and the employee’s share of Social Security and Medicare taxes. Paid leave under the FFCRA is treated like other paid leave for purposes of 401(k) plans and other benefits that an employer provides, and qualified leave wages would generally be considered wages for purposes of a benefits plan unless the plan provides otherwise.

[1] As discussed below, there are specific rules for determining whether an employer has fewer than 500 employees as well as when business entities should be treated as separate employers and when they should be aggregated as a single employer for purposes of determining whether they exceed

the 500-employee threshold. Under these rules, subsidiaries and other entities within a controlled group (as defined below) may be treated as separate

employers for purposes of determining whether a business has fewer than 500 employees.

[2] The U.S. Department of Health and Human Services (HHS) has not yet identified any “substantially similar condition” that would allow an employee to take paid sick leave. If HHS does identify any such condition, the Department of Labor will issue guidance explaining when an employee may take

paid sick leave on the basis of a “substantially similar condition.”

[3] 29 U.S.C. 826.20(a). As of April 7, 2020, 42 states had in place similar orders. See Sarah Mevrosch, Denise Lu, and Vanessa Swales, “See Which States and Cities Have Told Residents to Stay at Home,” N.Y. Times (Apr. 7, 2020), <https://www.nytimes.com/interactive/2020/us/coronavirus-stay-at-home-order.html>.

[4] Employers subject to the Railroad Retirement Tax Act are not subject to either Social Security tax or Medicare tax on the qualified leave wages; accordingly, they do not get a credit for Medicare tax.

[5] All section references are to the Internal Revenue Code and the U.S. Treasury regulations promulgated thereunder.

[6] U.S. Dep’t of Labor, “Families First Coronavirus Response Act: Questions and Answers”, U.S. Dep’t of Labor – Wages and Hour Division (2020), <https://www.dol.gov/agencies/whd/pandemic/ffcra-questions>.

[7] A controlled group exists where there is (1) one or more chains of corporations that are connected through stock ownership with a common parent corporation; 80% of the stock of each corporation, except the common parent, is owned by one or more corporations in the group, and the parent

corporation owns 80% of at least one other corporation; (2) a group of two or more corporations, in which five or fewer common owners (an individual, a

trust, or an estate) own directly or indirectly own 80% or more of the stock of each corporation and have identical ownership of more than 50% of the

stock of each corporation; or (3) a group of three or more corporations that are members of a group described in (1) or (2) above, and at least one of the

group members is the parent corporation of a group described in (1) and a member of a group described in (2). Section 1563(a); Treas. Reg. §

[8] This exemption applies if an authorized officer of the business has determined that (1) the provision of paid sick leave or expanded family and medical leave would result in the small business's expenses and financial obligations exceeding available business revenues and cause the small business to cease operating at a minimal capacity; (2) the absence of the employee or employees requesting paid sick leave or expanded family and medical leave would entail a substantial risk to the financial health or operational capabilities of the small business because of their specialized skills, knowledge of the business, or responsibilities; or (3) there are not sufficient workers who are able, willing, and qualified, and who will be available at the time and place needed, to perform the labor or services provided by the employee or employees requesting paid sick leave or expanded family and

[9] Section 45S provides employers with a tax credit for paid family and medical leave so long as the employer has a written policy under which it pays its employees at least 50% of their regular wages for at least two weeks of family and medical leave, and certain other requirements are satisfied.

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