COMPLIANCE BULLETIN

IRS Issues Guidance on State PFML Contributions, Benefits

The IRS has issued Revenue Ruling 2025-4, providing long-awaited guidance on the federal tax treatment of contributions and benefits under state paid family and medical leave (PFML) programs. The ruling addresses how federal income and employment tax rules apply to the programs and includes guidance on related reporting requirements. The guidance was issued Jan. 15, 2025.

The ruling is effective for payments made on or after Jan. 1, 2025, but transitional relief applies for payments during 2025.

Currently, 13 states and the District of Columbia have enacted mandatory PFML programs. The ruling does not address state PFML programs that are voluntary.

Highlights

- IRS Revenue Ruling 2025-4 addresses contributions and payments under mandatory state PFML programs.
- Generally, employers and employees may deduct their required PFML contributions.
- The guidance provides rules on whether benefit payments are included as employee income.
- Transitional relief applies to payments in 2025.

Action Steps

Employers should study the revenue ruling so they are prepared to comply with federal tax requirements for PFML contributions and payments.

In particular, employers should act to ensure that their payroll and W-2 form practices meet the withholding and reporting requirements detailed in the guidance.

The IRS is soliciting comments on additional situations and aspects of state PFML that are not covered in the revenue ruling. Employers may submit their written comments by April 15, 2025.

Important Dates

Jan. 15, 2025

IRS issued Revenue Ruling 2025-4, addressing the federal tax treatment of contributions and payments under mandatory state PFML programs. Certain transitional relief applies during calendar year 2025.

April 15, 2025

IRS deadline for comments on additional PFML issues.

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State Mandatory PFML Programs

In recent years, mandatory PFML programs have been enacted across the country, with 13 states and the District of Columbia having put in place PFML mandates to date. Additional states have established voluntary PFML programs, but the revenue ruling explicitly exempts these programs from its coverage.

State PFML programs vary as to features like employee eligibility requirements, covered employers, length of benefit coverage, amount of compensation, qualifying reasons for leave and job protections. Many state PFML laws also allow employers to meet their PFML obligations through an approved private PFML plan.

The IRS guidance discusses the rules it articulates in the context of a particular state PFML program ("State X"), whose described features are fairly standard, including funding from both employer contributions and employee payroll withholding at a set rate based on a percentage of employee wages, remitted to a state-administered fund.

The revenue ruling does **not** apply to private plans.

Federal Tax Treatment of PFML Contributions and Benefits

Employer Contributions

In general, according to the revenue ruling, employers may deduct their **mandatory** contributions to PFML programs as an excise tax. These amounts are not included in the federal gross income of the employee under IRS Code § 61.

State PFML laws often allow employers to **voluntarily** pay part or all of their employees' required contributions to the program. The ruling terms this an "employer pick-up" and allows the employer to deduct the payment as a business expense. The payments are treated as additional compensation to the employee under § 61 and included in wages for federal employment tax purposes. In addition, the employer must report the pick-up on the employee's Form W-2. However, the employee may deduct the employer pick-up as state income tax, but only if the employee itemizes their deductions and only up to the state and local income tax (SALT) deduction limit.

Employee Contributions

Employees may similarly deduct the PFML contributions that are withheld from their pay by their employer as an income tax payment, but again only if they itemize their tax deductions and only up to the SALT limit. Even though these amounts are withheld from the employee's wages, they are included in the employee's gross income, and the employer must report the contributions on the employee's Form W-2.

Benefit Payments

Generally, state paid **family leave** (as opposed to medical leave) payments must be included in employees' gross income. However, these amounts are **not** wages subject to federal employment taxes. Nonetheless, states must file with the IRS and provide employees with a Form 1099 for any paid family leave payments of $600 or more in a taxable year.

State **medical leave** payments are treated differently in the revenue ruling. For these benefits, only the portion of the payments attributable to the employer's contribution is included in the employee's gross income. This portion is also subject to both the employer's and employee's shares of Social Security and Medicare taxes. The amount of the medical leave payment attributable to the employee's portion of contributions is excluded from the employee's gross income and is not subject to Social Security or Medicare taxes.

Tables

The revenue ruling included the two tables below detailing the tax requirements of contributions and payments under state PFML programs.

Table 1. Summary of the Federal Income Tax Consequences of Contributions to State PFML Programs

Types of Contributions	Consequence to Employer	Consequence to Employee
Employer contribution	Employer may deduct the employer contribution as an excise tax under § 164 of the IRS Code.	Employee does not include the employer contribution in employee's federal gross income.
Employee contribution	Employer must include the employee contribution as wages on employee's Form W-2.	Employee contribution is included in employee's federal gross income as wages. Employee may deduct the employee contribution as state income tax under § 164 if employee itemizes deductions on employee's federal income tax return, but only to the extent the deduction for state tax paid does not exceed the SALT deduction limitation provided under § 164(b)(6).
Employer pick-up of employee contributions	Employer may deduct the employer pick-up payment that employer pays from employer's funds as an ordinary and necessary business expense under § 162. Employer must include the employer voluntary payment as wages on employee's Form W-2.	The employer pick-up is additional compensation to employee and is included in employee's federal gross income as wages. Employee may deduct the employer pick-up of the employee contribution as state income tax under § 164 if employee itemizes deductions on employee's federal income tax return, but only to the extent the deduction for state tax paid does not exceed the SALT deduction limitation provided under § 164(b)(6).

Table 2. Summary of the Federal Income Tax Consequences of Family and Medical Leave Benefits Paid by State PFML Programs

Type of Benefits	Amount Attributable to Employer Contribution	Amount Attributable to Employee Contribution
Family leave benefits	Employee must include the amount attributable to the employer contribution in employee's federal gross income (employer contribution not previously included in employee's federal gross income). This amount is not wages. State must file with the IRS and furnish employee a Form 1099 to report these payments.	Employee must include the amount attributable to the employee contribution, as well as to any employer pick-up of the employee contribution, in employee's federal gross income. This amount is not wages. State must file with the IRS and furnish employee a Form 1099 to report these payments.
Medical leave benefits	Employee must include the amount attributable to the employer contribution in employee's federal gross income (employer contribution not previously included in employee's federal gross income) except as otherwise provided in § 105. This amount is wages. The sick pay reporting rules apply to the medical leave benefits attributable to employer contributions. These payments are third-party payments (by a party that is not an agent of the employer) of sick pay.	The amount attributable to the employee contribution, as well as to any employer pick-up of the employee contribution, is excluded from employee's federal gross income.

Effective Dates

The revenue ruling states that it is effective for payments made on or after Jan. 1, 2025; however, the ruling provides the transition relief detailed below for payments made during calendar year 2025:

- **Medical leave benefit payments made in 2025 attributable to an employer's contribution**—States and employers are not required to follow the income tax withholding and reporting requirements applicable to third-party sick pay. Neither the state nor the employer will be liable for any associated penalties under Code § 6721 for failure to file a correct information return or under § 6722 for failure to furnish a correct payee statement to the payee.

- **Medical leave benefit payments made in 2025 attributable to an employer's contribution**—States and employers are not required to comply with § 32.1 and related Code sections (as well as similar requirements under § 3306) during the calendar year or to withhold and pay associated taxes; consequently, associated penalties will not apply.
- **Employer pick-up payments made during calendar year 2025**—Employers are not required to treat amounts they voluntarily pay for any part of an employee's required PFML contribution as wages for federal employment tax purposes under §§ 3121(a), 3306(b) and 3401(a).

Comments Requested

The IRS is soliciting comments on additional situations and aspects of state PFML programs that are not covered in Revenue Ruling 2025-4. The comments may be submitted electronically via the federal e-rulemaking portal at https://www.regulations.gov. Comments may also be submitted by mail to the following address: Internal Revenue Service, CC:PA:LPD:PR (Revenue Ruling 2025-4), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, D.C., 20044. Comments should be submitted in writing on or before April 15, 2025.