



Federal Paid Family and Medical Leave Tax Credit Expanded

What Employers Need to Know

Executive Summary

The Department of the Treasury and Internal Revenue Service recently issued Notice 2026-28, providing guidance on significant changes to the federal Paid Family and Medical Leave (PFML) Tax Credit under the Working Families Tax Cuts Act (WFTC).

The law permanently extends and expands the employer tax credit that was first established under IRC Section 45S. As a result of this extension, more employers may qualify for the credit and additional employees can be covered. For employers that offer paid family and medical leave, the updated rules may create valuable opportunities to offset the cost of providing benefits while supporting workforce recruitment, retention and well-being.

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Background

The federal Paid Family and Medical Leave Tax Credit was originally enacted to encourage employers to voluntarily provide paid leave benefits to employees who need time away from work due to their own serious health condition or to care for a qualifying family member.

The Working Families Tax Cuts Act makes the credit permanent and expands its availability beginning with the 2026 tax year. Employers that meet the program's requirements may continue to claim a general business tax credit equal to 12.5% to 25% of qualifying wages paid during eligible family and medical leave, for up to 12 weeks of leave per employee per year.

Key Enhancements Under the Working Families Tax Cuts Act

1. Expanded Employee Eligibility

Prior rules limited eligibility to employees meeting certain tenure and compensation requirements. Under the WFTC, employers may now claim the credit for:

- Employees with at least six months of service
- Certain part-time employees who customarily work at least 20 hours per week

This expansion makes it easier for employers with variable-hour, part-time and newer employees to qualify for the credit. Organizations with more diverse workforce populations may now be able to claim the credit on a broader segment of their employee population, increasing the overall value of the incentive.

2. Credit Available for Insurance Premiums

One of the most significant changes is the ability for employers to claim the credit based on premiums paid for qualifying PFML insurance policies, rather than solely on wages paid during leave.

Beginning in 2026, employers generally may choose between:

WAGE-BASED METHOD

Calculate the credit using qualifying wages paid to employees while they are on family or medical leave.

PREMIUM-BASED METHOD

Calculate the credit based on premiums paid for qualifying PFML insurance coverage.

Notice 2026-28 provides guidance regarding:

- How the premium method operates
- Allocation of qualifying premiums
- Election procedures between the wage-based and premium-based methods

This change may make the credit more accessible to employers that rely on insured leave programs rather than self-funded wage replacement arrangements. Employers should consult their tax advisors and insurance carriers to determine which approach may provide the greatest tax benefit.

3. Coordination with State and Local Paid Leave Programs

The law also provides clarification regarding the interaction between the federal credit and state or local paid leave mandates.

Under the WFTC:

- Leave provided pursuant to a state or local paid leave requirement may count toward meeting federal eligibility requirements
- However, leave that is mandated under state or local law generally cannot be included when calculating the amount of the federal tax credit

Employers operating in states with mandatory paid family or medical leave programs should carefully analyze which portions of their leave programs are employer-provided versus state-required. The distinction may affect both eligibility for and calculation of the available federal credit.

Why This Matters for Employers

The permanent expansion of the tax credit comes at a time when employers continue to face pressure to offer competitive leave benefits while managing costs.

Potential advantages include:

- Offsetting the cost of providing paid family and medical leave
- Supporting employee recruitment and retention efforts
- Enhancing employee well-being and financial security during periods of leave
- Increasing access to leave benefits for part-time and newer employees
- Providing flexibility through insured or wage-based program designs

For employers that do not currently provide paid family and medical leave beyond legal requirements, the expanded credit may warrant a re-evaluation of existing leave strategies.

Action Items for Employers

Employers should consider the following steps:

1. **Review Existing Leave Programs** – Evaluate whether current family and medical leave benefits satisfy Section 45S requirements and whether program design changes may increase eligibility for the credit.
2. **Analyze Employee Eligibility** – Determine how the reduced service requirement and expanded part-time employee eligibility affect potential credit availability.
3. **Assess Funding Methods** – Review whether a wage-based approach, insured PFML product, or combination of both may produce the most favorable outcome.
4. **Evaluate State Leave Integration** – Employers operating in states with mandatory paid leave programs should assess how those benefits coordinate with the federal credit and identify any employer-funded benefits that may qualify.
5. **Consult Tax and Benefits Advisors** – Notice 2026-28 provides initial guidance, but the Treasury Department and the IRS have indicated that proposed regulations are forthcoming. Employers should continue to monitor developments and seek professional advice regarding claiming the credit.

Alera Group Perspective

The expansion of the Section 45S tax credit may create new opportunities for employers to enhance paid family and medical leave offerings while reducing the financial burden of providing these benefits. Employers should work closely with their benefits, leave administration and tax advisors to evaluate whether current leave programs maximize available credits and align with evolving workforce expectations. By understanding the expanded eligibility rules, available funding methods and coordination requirements, employers can make informed decisions that support both compliance and employee well-being.



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