# A memo from the Massachusetts Department of Family and Medical Leave (DFML) regarding IRS Revenue Ruling 2025-4

The IRS has issued new tax guidance that will impact employers in Massachusetts. Starting on January 1, 2026, DFML and employers participating in state-run Paid Family and Medical Leave (PFML) programs must comply with new IRS tax and reporting requirements.

#### **Brief Overview**

- Certain portions of medical leave benefits will be treated like third-party sick pay (wages) starting on January 1, 2026.
- Employers with employees who receive medical leave benefits that are considered third-party sick pay will be responsible for remitting employer portions of FICA (Medicare and Social Security) and FUTA (federal unemployment) taxes on these benefits and reporting the benefits on the employee's Form W-2.
- ➤ DFML will provide employers with information about the benefits paid and the taxes withheld through the DFML Employer Portal. Employers should make sure that the appropriate personnel or entities have access to the Employer Portal to receive this important tax-related information.
- > State and federal income taxes on medical leave benefits that are considered third-party sick pay will be withheld at the option of the employee.
- There is no change in the treatment of family leave benefits. These benefits will be reported to employees and the IRS on Form 1099-G. Employees may choose whether to have state and federal income taxes withheld on family leave benefits.

### Details on IRS Revenue Ruling 2025-4

On January 15, 2025, the IRS issued Revenue Ruling 2025-4 ("the Ruling"). The Ruling is the first comprehensive guidance from the IRS on the federal income and employment tax treatment of PFML benefits and contributions to state PFML programs.

Although the Ruling is effective as of January 1, 2025, the IRS has announced calendar year 2025 (January 1 – December 31) as a transition year for enforcement and administration of the new reporting requirements. **IRS enforcement of the Ruling will begin in 2026.** 

### What Employers Need to Know about the Ruling

Employers should refer to the <u>guidance from the IRS</u> and work with a tax professional to understand their responsibilities under the Ruling. Whether PFML benefits are taxable will depend on the type of leave taken and <u>employer and employee contributions</u>.

**DFML** is providing the following information to help employers prepare for compliance with the Ruling beginning on January 1, 2026. Employers are responsible for complying with all applicable laws, rules, and guidelines.

### **Family Leave Benefits**

The Ruling will not change the tax treatment or reporting of family leave benefits by DFML.

- Family leave (100%) benefits are subject to federal and state income taxes, but not federal employment taxes.
- Family leave benefits are analogous to Social Security payments. These benefits are includable in Federal gross income but not considered wages.
- Federal and state income tax withholding will remain optional for family leave benefits.
- DFML will provide a Form 1099-G to employees for family leave benefits paid through the PFML program.

#### **Medical Leave Benefits**

The Ruling outlines important changes for the tax treatment and reporting of medical leave benefits.

- Starting January 1, 2026, DFML will determine the taxability of medical leave benefits depending, in part, on an employer's workforce size. According to the Ruling, the portion of PFML contributions that an employer is required to pay for medical leave benefits will determine the portion of medical leave benefits that will be subject to federal income tax, state income tax, and employment taxes.
- Under Massachusetts law, employers with 25 or more employees are required to pay at least 60% of the medical contribution. Only the benefit amount attributable to the required employer contribution (60%) will be subject to federal income tax, state income tax, and employment taxes.

- Medical leave benefits attributable to the employee contribution (including any employer pick-up) are not subject to federal income tax, state income tax, or employment taxes.
- For employers with fewer than 25 employees, employees pay 100% of the medical contribution. Therefore, medical leave benefits paid to these employees are not subject to income or employment taxes.
- Medical leave benefits are analogous to disability payments. Amounts attributable
  to employer contributions are includable in Federal gross income and are
  considered wages. Amounts attributable to employee contributions are excluded
  from Federal gross income and are not wages.
- DFML will withhold the employee portion of FICA taxes on taxable medical benefits, unless the employer is exempt from social security and/or Medicare taxes.
- DFML will also provide notice to employers regarding the medical benefits paid and taxes withheld, in compliance with the Ruling and other tax guidance.
- Employers with 25 or more employees will be required to pay the employer portion of FICA and FUTA taxes for employees who receive taxable medical leave benefits from DFML.

## Important Guidance for Employers Participating in the MA PFML Program

### New guidance following the Ruling:

- Starting January 1, 2026, DFML will withhold the employee's portion of FICA taxes on taxable medical leave benefit payments and report benefits and tax information to employers. Employers will be responsible for paying the employer share of FICA, as well as all FUTA taxes.
- Employers should consult tax professionals and/or their payroll provider about how these changes may affect the way they file their Employer's Quarterly Federal Tax Return (Form 941), Form W-2, and other applicable federal and state tax reporting obligations for these benefits.
- Employers with 25 or more employees will need to report taxable medical leave payments on employee Form W-2, Wage and Tax Statements.
- DFML will report the taxable portion of medical leave benefits and taxes withheld to employers on the Employer Portal so they can fulfill their obligations under the Ruling. This will enable employers to pay their share of FICA and FUTA taxes and include the taxable portion of medical benefits as wages on employee W-2 forms.

DFML plans to make benefit information and related tax details available to
employers on the Employer Portal website. Employers should make sure that the
appropriate payroll personnel or entities have access to the Employer Portal to
receive this important tax-related information. Keep an eye out for updates on the
availability of this information. If you do not have a Leave Administrator registered
with DFML, you should take steps now to get access.

### Guidance that remains unaffected by the Ruling:

- Federal income tax and state income tax withholding from DFML benefit payments
  will remain optional for medical and family leave benefits. However, for individuals
  who take medical leave from employers who have 25 or more employees and
  choose to withhold income taxes, DFML will only withhold taxes on 60% of the
  medical benefit, in compliance with the Ruling.
- At this time, medical leave benefits for employees working for employers with fewer than 25 employees are not subject to federal income tax, state income tax, or employment taxes. DFML will not withhold taxes on medical leave benefits for individuals who take leave from employers with fewer than 25 employees.

### Guidance for Employers with Exemptions for Purchased Private Plans or Self-Insured Plans

The Ruling applies only to state-run PFML programs. It does not address federal tax treatment of private or self-insured PFML plans. Employers with an approved exemption for a private or self-insured PFML plan should consult with third party administrators, insurance carriers, tax professionals, or legal counsel to determine tax treatment and reporting obligations under state and federal law.

### Guidance for Self-Employed Individuals

Self-employed individuals should consult with tax professionals to determine tax treatment and reporting obligations under state and federal law.

### **Appendix**

The following tables are excerpted from IRS Revenue Ruling 2025-4.

Table 1. Summary of the Federal Income Tax Consequences of Contributions to State Paid Family and Medical Leave Programs

Types of contributions	Consequence to employer	Consequence to employee
Employer	Employer may deduct the	Employee does not include the employer
contribution	employer contribution as an	contribution in employee's Federal gross income.
	excise tax under § 164.	
Employee	Employer must include the	The employee contribution is included in employee's
contribution	employee contribution as wages	Federal gross income as wages.
	on employee's Form W-2.	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	Employer may deduct the	The employer pick-up is additional compensation to
of employee	employer pick-up payment that	employee and is included in employee's Federal gross
contributions	employer pays from employer's	income as wages.
	funds as an ordinary and	Employee may deduct the employer pick-up of the
	necessary business expense	employee contribution as State income tax under §
	under § 162.	164, if employee itemizes deductions on employee's
	Employer must include the	Federal income tax return, but only to the extent the
	employer voluntary payment as	deduction for State tax paid does not exceed the SALT
	wages on employee's Form W-2.	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 Paid Family and Medical Leave 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 to 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 to 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, are excluded from employee's Federal gross income.