Part I

Section 164.—Taxes

26 CFR 1.164-1: Deduction for Taxes.
(Also: §§ 61, 162, 104, 105, 106, 3121, 3306, 3401, 6041, 6051, 7805, 1.61-1, 1.61-2, 301.7805-1)

Rev. Rul. 2025-4

ISSUES

What is the Federal income and employment tax treatment of contributions and benefits paid in certain situations under a State paid family and medical leave (PFML) statute, and what are the related reporting requirements?

FACTS

In 2021, State X enacted the State X Paid Family and Medical Leave Act (PFML Act), which became effective in State X on January 1, 2022. The PFML Act implemented a State-administered family and medical leave program to provide wage replacement to workers for periods in which they need to take time off from work due to

their own non-occupational injuries, illnesses, or medical conditions, or to care for a family member due to the family member's serious health condition or other prescribed circumstance. The PFML Act indicates that the purpose of the statute is to provide a safety net for all employees in State X when they have personal or family caregiving needs and to advance the public interest by promoting the health, safety, and welfare of all residents of State X.

To fund State X's provision of benefits under the PFML Act, all in-state employers and employees are required to make contributions with respect to each employee to the State X Paid Family and Medical Leave Fund (PFML Fund) operated and administered by State X. State X collects these contributions from employers and deposits them into the PFML Fund for the purpose of providing the family and medical leave benefits described under the PFML Act to individuals covered by the PFML Act. These contributions must be equal to a specified percentage of each employee's weekly wages (computed in accordance with the PFML Act), referred to as the "standard contribution rate." The State X Director of Employment determines the State X standard contribution rate for each plan year, which is based on the calendar year, before the beginning of such calendar year. For 2025, the State X standard contribution rate is set at 1% of each employee's weekly wages.[1]

Under the PFML Act, employers with employees in State X are required to withhold and remit contributions from each employee's wages in an amount that is no greater

[1] While the State X PFML Act imposes a single contribution rate to a fund for both family and medical leave benefits, some States impose different contribution rates for remittance into separate family and medical leave funds.

than 60% of the standard contribution rate (1%) multiplied by each employee’s weekly wages. The PFML Act also provides that these employers must make contributions from their own funds in an amount that is equal to 40% of the standard contribution rate (1%) multiplied by each employee’s weekly wages.[2] By operation of these rules, an employer may voluntarily pay from its own funds all or a portion of its employees’ otherwise mandatory contributions, rather than withholding such amounts from the employee’s wages (“employer pick-up”). Under State X law, an employer pick-up is not included in the employee’s wages for purposes of determining the employee’s weekly wages under the PFML Act.

As an alternative to employer and employee contributions to the PFML Fund, the PFML Act provides an option whereby an employer may establish and maintain a private plan for the payment of family and medical leave benefits. An employer establishing such a plan must submit the plan for approval to the State X Director of Employment. The plan must provide employee benefits that are comparable to those required under the PFML Act, and the benefits must be available at a cost to employees not to exceed the contributions otherwise required under the PFML Act. Employees whose employer maintains an approved private plan are eligible for benefits only from the private plan.[3]

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[2] Some State PFML statutes specify different contribution ratios for employers and employees depending on the size of the employer. The analysis in this revenue ruling would also apply to those situations.

[3] This revenue ruling does not address the Federal tax treatment of employers’ or employees’ contributions to private or self-insurance family or medical leave plans or the amounts received by the employees as benefits under these plans.

The PFML Act provides wage replacement for qualifying family and medical leave to any individual who earned at least $2,500 from an employer for services as an employee in State X during each of four of the five quarters completed immediately prior to the period of leave (“eligible employee”). The PFML Act defines qualifying family leave as time off from work taken by an eligible employee for any of the following conditions or events: (1) to care for and bond with a child during the first year after the child’s birth or during the first year after the placement of the child through foster care or adoption; (2) to care for a family member (*i.e.*, a child, spouse, parent, grandparent, grandchild, sibling, or domestic partner) with a serious health condition; (3) to deal with certain qualifying exigencies defined by State X law related to the covered active duty or call to covered active duty of the individual’s spouse, domestic partner, child, or parent in the Armed Forces of the United States; and (4) to address certain medical or non-medical needs of an eligible employee’s child, spouse, parent, grandparent, grandchild, sibling, or domestic partner arising from domestic violence. The PFML Act defines qualifying medical leave as time off from work taken by an eligible employee that is made necessary by the individual’s own serious health condition and requires the health condition to be substantiated. The PFML Act does not require that an employee incur any medical expenses in order to be eligible for medical leave benefits, and State X does not collect any information from employees related to any medical expenses that an employee might have incurred.

Under the PFML Act, an eligible employee’s “weekly benefit amount” for periods of qualifying family or medical leave taken on or after January 1, 2025, is equal to 80% of

the employee's average weekly wages as defined in the PFML Act. Eligible employees can receive family leave or medical leave benefits, up to 12 weeks each, during the application year (the 12-month period beginning with when the employee applies for PFML benefits). Family leave benefits and medical leave benefits may not be provided concurrently to an eligible employee but may be taken during consecutive periods.

Situation 1. Employer's and Employee's Contributions. Employer A is a corporation that employs 100 individuals in State X, including Employee B. Employer A uses the accrual method of accounting and the calendar year as the taxable year for Federal income tax purposes. Employee B is an individual residing in State X. Employer A employs Employee B for the entire 2025 calendar year. For 2025, Employee B's weekly wages as defined under the PFML Act are $2,000, totaling $104,000 for the calendar year, as computed in accordance with the PFML Act. Because State X set the standard contribution rate for 2025 at 1% of each employee's weekly wages, Employer A remits a total of $1,040 to the State X PFML Fund in connection with Employee B's employment. Of this total, and as required by the PFML Act, during 2025 Employer A withholds and remits $624 from Employee B's wages and pays the remaining $416 out of its own funds.

Situation 2. Family Leave Benefits. Same facts as in *Situation 1*, except that beginning in March 2026, Employee B takes 12 weeks off as a result of one of the conditions or events specified for family leave under the PFML Act. Employer A continues to employ Employee B at $2,000 per week in 2026, and Employee B meets all other eligibility requirements under the PFML Act. Therefore, Employee B qualifies to

receive up to 12 weeks of family leave benefits from State X in an amount equal to 80% of Employee B's average weekly wage calculated at the beginning of Employee B's period of family leave, that is, $1,600 ($2,000 X 80%) per week. In 2026, Employee B takes no other types of leave covered by the PFML Act. Accordingly, State X pays Employee B a total of $19,200 ($1,600 per week X 12 weeks) in family leave benefits in 2026.

Situation 3. Medical Leave Benefits. Same facts as in Situation 1, except that beginning in March 2026, Employee B takes 12 weeks off as a result of Employee B's serious health condition that qualifies for medical leave benefits under the PFML Act. Employer A continues to employ Employee B at $2,000 per week in 2026, and Employee B meets all other eligibility requirements under the PFML Act. Therefore, Employee B qualifies to receive up to 12 weeks of medical leave benefits from State X in an amount equal to 80% of Employee B's average weekly wage calculated at the beginning of Employee B's period of medical leave, that is, $1,600 ($2,000 X 80%) per week. In 2026, Employee B takes no other types of leave covered by the PFML Act. Accordingly, State X pays Employee B a total of $19,200 ($1,600 per week X 12 weeks) in medical leave benefits in 2026.

Situation 4. Employer Pick-Up of Employee Contributions. Same facts as in *Situation 1*, except that, as permitted under the PFML Act, Employer A withholds and remits $350 from Employee B's wages, an amount less than the $624 that Employer A is otherwise required to withhold from Employee B's wages. Employer A voluntarily pays from its own funds the remaining $274 of the employee's otherwise required

contribution amount, as an "employer pick-up," as well as the $416 that Employer A is required to pay under the PFML Act.

Situation 5. Family Leave Benefits with Employer Pick-Up of Employee Contributions. Same facts as in *Situation 2*, except that, as in *Situation* 4, Employer A withholds and remits $350 from Employee B's wages in 2025, an amount less than the $624 that it is otherwise required to withhold from Employee B's wages, and voluntarily pays the difference from its own funds.

Situation 6. Medical Leave Benefits with Employer Pick-Up of Employee Contributions. Same facts as in *Situation 3* except that, as in *Situation 4*, Employer A withholds and remits $350 from Employee B's wages in 2025, an amount less than the $624 that it is otherwise required to withhold from Employee B's wages, and voluntarily pays the difference from its own funds.

LAW

(1) Federal Income Tax Treatment of Mandatory Contributions to Certain State Funds

Section 162 provides a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered. *See* § 1.162-7.[4]

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[4] Unless otherwise specified, all "section" or "§" references are to sections of the Code or the Treasury Regulations.

Subject to certain limitations,[5] § 164(a)(3) permits a taxpayer to claim a deduction for certain State, local, and foreign income taxes paid or accrued during the taxable year. Under the flush language of § 164(a), a taxpayer may also deduct taxes incurred in carrying on a trade or business activity. Generally, taxes may be deducted only by the taxpayer upon whom that tax is imposed. Section 1.164-1(a); *Armentrout v. Commissioner*, 43 T.C. 16, 19-21 (1964).

As a general rule, "[t]he intention of Congress controls what law, federal or state, is to be applied . . . Since the federal revenue laws are designed for a national scheme of taxation, their provisions are not to be deemed subject to state law 'unless the language or necessary implication of the section involved' so requires." *Helvering v. Stuart*, 317 U.S. 154, 161 (1942) (quoting *United States v. Pelzer*, 312 U.S. 399, 402-03 (1941)). Thus, principles developed under Federal law, not State interpretations or designations, determine whether a payment to the State or its instrumentality falls within the meaning of the terms "taxes" or "income taxes" for purposes of § 164. *See* Rev. Rul. 79-180, 1979-1 C.B. 95; Rev. Rul. 76-215, 1976-1 C.B. 194; Rev. Rul. 71-49, 1971-1 C.B. 103; Rev. Rul. 61-152, 1961-2 C.B. 42. For these purposes, a tax has been defined as a mandatory, compulsory exaction or levy imposed upon a taxpayer by the legislative

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[5] Under § 63 an individual can claim itemized deductions, such as the deduction under § 164 for certain state and local taxes, only if the individual elects to itemize deductions on that individual's Federal individual income tax return. Generally, if the individual does not elect to itemize deductions, the individual will be limited to the deductions listed in § 63(b), including the standard deduction. Further, even if an individual elects to itemize deductions, § 164(b)(6), as added by § 11042(a) of Public Law 115-97, 131 Stat. 2054 (December 22, 2017), commonly referred to as the Tax Cuts and Jobs Act, limits an individual's itemized deduction under § 164(a) (SALT deduction limitation) to $10,000 ($5,000 in the case of a married individual filing a separate return) for the aggregate amount of certain "State and local taxes" paid during the calendar year. This SALT deduction limitation applies to taxable years beginning after December 31, 2017, and before January 1, 2026.

body of a State or locality for the purpose of generating government revenue. *See Principal Life Ins. Co. v. United States*, 70 Fed. Cl. 144, 167-69 (2006); *see also* Rev. Rul. 75-444, 1975-2 C.B. 66 (a tax is an "enforced contribution, exacted pursuant to legislative authority"). In this sense, taxes are distinct from other levies and fees that are imposed upon particular taxpayers as a charge for the government's provision of a particular service or asset or grant of a narrow benefit or right to those taxpayers. *Id.* Thus, the courts have held that taxes are those exactions that operate to distribute among the general public the burden and cost of government operations and programs that benefit the public-at-large. *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 622-23 (1981). While a tax must be paid to the government levying the tax, an enforced contribution may be characterized as a tax within the purview of § 164 even if it is paid into a separate fund established by the State rather than to the State's general fund if the separate fund is established for public purposes and is used to discharge a government function. *See*, *e.g.*, Rev. Rul. 81-191, 1981-2 C.B. 49; Rev. Rul. 74-525, 1974-2 C.B. 411; Rev. Rul. 74-58, 1974-1 C.B. 180; and Rev. Rul. 71-49. Also, the courts have clarified that the nature of an otherwise mandatory tax will not be altered by the State legislature's decision to provide its taxpayers with a discretionary alternative to the tax or to provide narrow exemptions therefrom. *Trujillo v. Commissioner*, 68 T.C. 670, 673-75 (1977) (holding that mandated employee contributions to California State disability fund are properly characterized as income taxes under § 164(a)(3) even though the State statute exempts certain employees from its mandates, including employees whose employers have established a private disability plan).

When a tax is tied to the occasion of a taxpayer's income, and the amount of that tax is determined as a factor thereof, such a tax is an "income" tax within the meaning of § 164(a)(3). *Id*. at 672; *McGowan v. Commissioner*, 67 T.C. 599, 608-11 (1976) (a tax on wages is simply a tax on a narrow band of the broad category of gross income, and is still an income tax). In addition, the IRS has held that a compulsory contribution of a percentage of gross wages imposed on employees required to be withheld from employees' salaries qualified as State income tax to employees under § 164(a)(3). *See* Rev. Rul. 89-16, 1989-1 C.B. 76 (amounts withheld from the wages of employees for contribution to the West Virginia Unemployment Compensation Trust Fund qualify as State "income taxes" and, therefore, are deductible by the employees under § 164(a)(3)).[6]

In contrast, taxes imposed by the State on the exercise of a privilege or the performance of a particular act—such as a business transaction, consumption, or manufacture or sale of certain commodities—are generally treated as excise taxes. *See, e.g., Flint v. Stone Tracy Co.*, 220 U.S. 107, 158 (1911); *Waxenberg v. Commissioner*, 62 T.C. 594, 603 (1974). Excise taxes are deductible under § 164 if they are paid or accrued in the carrying on of a trade or business, or other profit-seeking activity. *See* § 164(a) (flush language); Rev. Rul. 81-194, 1981-2 C.B. 54 (amounts paid

[6] The fact that the amounts are withheld from an employee's wages by the employer, rather than first being remitted to the employee to pay the tax directly, does not affect the amount of income arising from such wages. *See*, *e.g.*, *Cohen v. Commissioner*, 63 T.C. 267, 278-79 (1974), *aff'd*, 543 F.2d 725 (9th Cir. 1976) (holding that amounts withheld from employee's pay under Civil Service Retirement Act were part of the employee's compensation); *Tucker v. Commissioner*, 69 T.C. 675, 678-79 (1978) (holding that employee was in receipt of taxable income when fine was deducted directly from salary rather than collected after employee was paid).

or accrued by employers to the California unemployment compensation and disability funds are State excise taxes and may be deducted under § 164(a) as taxes paid or accrued in carrying on a trade or business).

In 1981, the IRS issued guidance on the treatment of employees' and employers' contributions to temporary and non-occupational disability benefit programs enacted in California, New Jersey, New York, and Rhode Island. *See* Rev. Rul. 81-194 (California); Rev. Rul. 81-193, 1981-2 C.B. 52 (New Jersey); Rev. Rul. 81-192, 1981-2 C.B. 50 (New York); Rev. Rul. 81-191 (Rhode Island). In general, these revenue rulings address State statutes that provide weekly disability benefits based upon average weekly wages to qualifying individuals who are totally disabled and unable to perform any work for remuneration as a result of an accident or sickness not compensated under the workers' compensation laws. Also, under these State statutes, both employers and employees are required to make contributions to the respective State's disability fund from which the State would provide these benefits. For the employee's contributions, the employer is required to withhold the employee's required contribution from the employee's wages at the time the wages are paid. In addition, three of these State statutes provide employers an alternative to the State's disability benefit program whereby an employer is permitted to establish and maintain self-insurance or a private plan for the payment of disability leave benefits.

Under these revenue rulings, the IRS holds that State-mandated employee and employer contributions to these disability funds are properly characterized as taxes levied by the respective State governments under § 164. Specifically, the rulings

conclude that mandatory amounts withheld by an employer from an employee's wages are treated as the employee's payment of State income taxes and are deductible by the employee under § 164(a)(3). The rulings also conclude that mandatory contributions paid by the employer with its own funds are characterized as State excise taxes paid or incurred in carrying on a trade or business and are deductible by the employer under the flush language of § 164(a).

(2) Federal Income Tax Treatment of Certain Payments and Benefits

Section 61(a) provides that, except as otherwise provided in subtitle A of the Code, gross income for Federal income tax purposes "means all income from whatever source derived" (Federal gross income). *See also* § 1.61-1(a); § 1.61-2(a). The U.S. Supreme Court has held that Federal gross income includes "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." *Commissioner v. Glenshaw Glass Co*., 348 U.S. 426, 431 (1955).

State excise taxes required to be paid to a State directly by an employer as a result of the employer's own liability for such taxes are not included in the employee's gross income under § 61. In contrast, amounts that are required to be withheld from an employee's wages and remitted by an employer to the State to satisfy the employee's State tax liability are includible in the employee's Federal gross income under § 61. *See* § 1.61-2(a)(1). Similarly, where an employer voluntarily pays a tax that is the responsibility of the employee, such as the employee's share of Federal Insurance Contributions Act (FICA) tax, without deducting it from the employee's wages, these amounts are included in the employee's gross income. *See* § 1.61-14(a) (another

person's payment of the taxpayer's income tax constitutes gross income to the taxpayer unless excluded by law); *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716, 729 (1929) (employer's payment of employee's income tax obligation in consideration of employee's services for employer constitutes income to employee); Rev. Rul. 86-14, 1986-1 C.B. 304 (payments by employer of employee's taxes are additional wages for FICA purposes, are includible in employee's gross income, and are wages for purposes of income tax withholding).

The Code provides various exclusions from gross income.[7] Section 104(a)(3) provides that, except in the case of amounts attributable to (and not in excess of) medical expense deductions allowed under § 213 for any prior taxable year, gross income does not include amounts received through accident or health insurance (or through an arrangement having the effect of accident or health insurance) for personal injuries or sickness (other than amounts received by an employee to the extent such amounts are attributable to contributions by the employer which were not includible in the gross income of the employee, or are paid by the employer).

Section 105(a) provides that amounts received by an employee through accident or health insurance for personal injuries or sickness must be included in gross income, except as otherwise provided in § 105, to the extent such amounts (1) are attributable to contributions by the employer which were not includible in the gross income of the employee, or (2) are paid by the employer.

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[7] Exclusions from income are construed narrowly, and taxpayers must bring themselves within the clear scope of an exclusion. *Commissioner v. Schleier*, 515 U.S. 323, 328 (1995).

Section 105(b) provides that, except in the case of amounts attributable to (and not in excess of) deductions allowed under § 213 for any prior taxable year, gross income does not include amounts referred to in § 105(a) if such amounts are paid, directly or indirectly, to the taxpayer to reimburse the taxpayer for expenses incurred for the medical care (as defined in § 213(d)) of the taxpayer, the taxpayer’s spouse, and the taxpayer’s dependents and children (as defined therein).

Section 105(e)(2) provides that, for purposes of §§ 105 and 104, amounts received from a sickness and disability fund for employees maintained under the law of a State or the District of Columbia are treated as amounts received through accident or health insurance.

The portion of the amounts received under an accident or health plan that is financed partially by an employer and that are attributable to employer contributions is determined under the rules of § 1.105-1(c)-(e). Generally, in the case of individual insured arrangements, the portion of the amount received by the employee attributable to the employer’s contribution is the amount that bears the same ratio to the amount received as the portion of the premiums paid by the employer for the current policy year bears to the total premiums paid by the employer and employee for the policy year. Section 1.105-1(d)(1).

In 1972 and 1975, the IRS issued guidance on the treatment of temporary and non-occupational disability benefit payments under the program enacted in New York. *See* Rev. Rul. 72-191, 1972-1 C.B. 45; Rev. Rul. 75-499, 1975-2 C.B. 43. The guidance held that the employer contributions are excluded from employees’ gross incomes, and that

the benefits received by current employees are therefore includible in their gross incomes under § 105 except as otherwise provided in that section, but are excluded from their gross incomes under § 104(a)(3) to the extent they are attributable to the employees' own contributions. *See also* Rev. Rul. 75-479, 1975-2 C.B. 44 (similar holding relating to Hawaii program).[8]

(3) Federal Employment Tax Requirements

Sections 3101 and 3111 impose FICA taxes on "wages," as that term is defined in § 3121(a). These taxes are imposed both on the employer under § 3111(a) and (b) and on the employee under § 3101(a) and (b). Section 3121(a) generally defines "wages" for this purpose as all remuneration for employment including the cash value of all remuneration (including benefits) paid in any medium other than cash. Section 3121(b) defines "employment" for FICA purposes as any service, of whatever nature, performed by an employee for the person employing him, with certain specific exceptions. These definitions are deliberately broad. *United States v. Quality Stores, Inc.*, 572 U.S. 141, 146 (2014); *Social Security Bd. v. Nierotko*, 327 U.S. 358, 365-66 (1946). Rules similar to the FICA rules apply with respect to Federal Unemployment Tax Act (FUTA) tax under §§ 3301, 3306(b), and 3306(c).

Section 3121(a) contains certain limited exceptions from wages for payments from employment-based plans and other arrangements. Section 3121(a)(2)(A), for example, excludes any payment to an employee on account of sickness or accident disability

[8] Rev. Rul. 81-192 modified the portion of Rev. Rul. 72-191 relating to the deductibility of contributions by the employer, but it did not modify the portion of the ruling relating to the taxability of benefit distributions or any other portion of the ruling.

received under a workers' compensation law, and § 3121(a)(4) excludes any payment on account of sickness or accident disability received more than 6 calendar months after the last calendar month in which the employee worked. Pub. L. No. 97-123, 95 Stat. 1659 (1981), eliminated the FICA exception for payments from an employer plan on account of sickness or accident disability. The legislative history states that "for purposes of the taxes imposed by this provision, payments made under a state temporary disability insurance law shall be treated as remuneration for service." H.R. Conf. Rep. No. 97-409, 14 (Dec. 14, 1981). Thus, unless they are excluded under § 3121(a)(2) or § 3121(a)(4), disability leave benefit payments like those described in Rev. Rul. 72-191 are FICA wages to the extent they are includible in gross income under § 105(a) and the regulations thereunder. Section 32.1(d)-(e). There is no comparable rule for family leave benefits under laws like the PFML Act. The same principles apply with respect to FUTA tax.

Section 3402(a) generally requires every employer making a payment of "wages," as that term is defined in § 3401(a), to deduct and withhold from these wages a tax determined in accordance with prescribed tables or computational procedures. Section 3401(a) defines "wages" for this purpose as all remuneration for services performed by an employee for the employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash, with certain specific exceptions. Wages generally include all payments by an employer of amounts includible in gross income under § 105(a) and § 1.105-1 to an employee under an accident or health plan for a period of absence from work on account of personal injuries or sickness. However,

third-party payments of sick pay, as defined in § 3402(o) and the regulations thereunder, are not wages under § 3401 or § 31.3401(a)-1, and therefore are not subject to income tax withholding even if they are includible in gross income. Section 31.3401(a)-1(b)(8)(i)(a); *see also* § 31.3402(o)-3(h).[9] Instead, employees may request withholding on a voluntary basis under § 3402(o). S*ee also* § 31.3402(o)-3(a). There are no comparable rules for third-party payments of family leave benefits under laws like the PFML Act.

(4) <u>Information Reporting Requirements</u>

Section 6041(a) generally requires that all persons engaged in a trade or business and making payment in the course of such trade or business to another person of rent; salaries; wages; premiums; annuities; compensations; remunerations; emoluments; or other fixed or determinable gains, profits, and income, of $600 or more in any taxable year, must make a true and accurate return to the Secretary of the Treasury or her delegate (Secretary).

Section 6041(d) provides that every person required to make a return under § 6041(a) must furnish to each person with respect to whom such return is required a written statement showing the name, address, and phone number of the person required to make such return, and the aggregate amount of payments to the person required to be shown on the return. Section 1.6041-1(b)(1) provides that the term "all persons engaged in a trade or business," as used in § 6041(a), includes organizations

[9] Payments are considered made by the employer if a third party makes the payments as an agent of the employer. Section 31.3401(a)-1(b)(8)(i)(b).

the activities of which are not for the purpose of gain or profit. Thus, that term includes the organizations referred to in § 1.6041-1(i). Section 1.6041-1(i) provides that the United States or a State, or political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing must file information returns on the Form 1099 Series to report certain payments of $600 or more. The information returns must be made by the officer or employee having control of such payments or by the officer or employee appropriately designated to make such returns. *See* § 1.6041-1(i). If the State has a basis for calculating the amount of its payment that is income to the payee, it must report that amount. *See* § 1.6041-1(c).

Section 6051(a) provides that every person required to deduct and withhold from an employee a tax under § 3101 or 3402, or who would have been required to deduct and withhold a tax under § 3402 (determined without regard to subsection (n)) if the employee had claimed no more than one withholding exemption, or every employer engaged in a trade or business who pays remuneration for services performed by an employee, shall furnish to each such employee in respect of the remuneration paid by such person to such employee during the calendar year, on or before January 31 of the succeeding year, a written statement showing the employee's wages, amounts of tax withheld, and certain other information. *See also* § 31.6051-1(a). Form W-2, *Wage and Tax Statement*, is used by employers to report to the employee these payments of wages, other remuneration for services performed by the employee, and amounts of tax withheld. Section 6051(d) provides that a duplicate of any statement made pursuant to § 6051 and in accordance with regulations prescribed by the Secretary shall, when

required by regulations, be filed with the Secretary. Section 31.6051-2(a) generally provides that an employer must file with the Social Security Administration a copy of each Form W-2 required under § 31.6051-1 to be furnished by the employer with respect to wages paid during the calendar year. *See also* §§ 6051(f) and 31.6051-3 for statements required in case of sick pay paid by third parties rather than employers and Notice 2015-6, 2015-5 I.R.B. 412, regarding the reporting of employment taxes with respect to sick pay paid by third parties.

ANALYSIS

Situation 1. Employer's and Employee's Contributions. The $624 that Employer A withholds from Employee B's wages and the $416 that Employer A pays from its own funds are properly characterized as State taxes because they are enforced contributions, exacted pursuant to State X's legislative authority in the exercise of its taxing power and imposed and collected by State X for the purpose of raising revenue for public purposes. Even though these amounts are not remitted into State X's general fund, they may be treated as taxes under § 164 because they are paid to a separate fund established by State X for public purposes and used to discharge a government function.

The $624 that Employer A withholds from Employee B's wages is tied to Employee B's receipt of wages and is determined as a factor thereof. As such, this amount is an income tax within the meaning of § 164(a)(3). Employee B may deduct this amount as a State income tax under § 164(a)(3) in 2025, the taxable year in which such amount is withheld from Employee B's pay. However, this deduction is available only if Employee

B itemizes these State taxes on Employee B's 2025 Federal income tax return, and only to the extent such deduction does not exceed the SALT deduction limitation provided under § 164(b)(6). Even though this amount is withheld from Employee B's wages, because it satisfies Employee B's own tax liability under the PFML Act, this amount is included in Employee B's gross income (and wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a)), and Employer A must report it on Employee B's Form W-2 in accordance with § 6051, for 2025.[10]

The $416 that Employer A pays from its own funds is required because of Employer A's status as an employer under the PFML Act and because the payment is incurred in carrying on Employer A's business. As such, Employer A may deduct this amount under § 164(a) (flush language) as an excise tax paid or accrued in carrying on its trade or business. This amount is not included in Employee B's gross income for 2025 under § 61 because it satisfies Employer A's own tax liability under the PFML Act, and therefore Employee B does not realize any accession to wealth from the payment. As such, Employer A has no Federal information reporting obligations with respect to this amount.

Situation 2. Family Leave Benefits. The $19,200 that State X pays to Employee B as family leave benefits under the PFML Act is included in Employee B's Federal gross

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[10] Some States' PFML statutes provide that if an employer fails to withhold any part of the employee's mandatory contribution from their pay, or if an employer fails to timely remit such contributions to the State, then the employer is held liable for the employee's share of such contribution. The inclusion of this or a similar provision in a State's PFML statute would not change the tax treatment of the employer's or employee's contributions in the situations described in this revenue ruling. Further, this revenue ruling does not address the tax treatment of contributions or benefits in situations in which those provisions are triggered.

income under § 61 because it provides Employee B with a clearly realized accession to wealth and no exclusion applies.[11] None of the family leave benefits paid to Employee B pursuant to the PFML Act are excluded from gross income under § 104(a)(3) because family leave benefits under the PFML Act may be paid to an eligible employee, for the benefit of the eligible employee, for a variety of conditions or events that are unrelated to the employee's own health condition, and the family leave benefits that are paid to Employee B are, in fact, paid for reasons unrelated to Employee B's own health condition. Therefore, those family leave benefits are not received from a sickness and disability fund for employees within the meaning of § 105(e)(2), are not paid for personal injuries or sickness, and as a result, for purposes of §§ 104 and 105, cannot be treated as amounts received through accident or health insurance.

Although the entire $19,200 that State X pays to Employee B as family leave benefits is included in Employee B's gross income for Federal income tax purposes, it does not constitute wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a), and is neither sick pay, as defined in § 3402(o), nor a disability leave benefit payment like those described in Rev. Rul. 72-191. Rather, family leave benefits are more closely analogous to social security benefits partially included in gross income under § 86 but not considered to have been paid as remuneration from

[11] Section 85 provides that gross income includes unemployment compensation, which generally means any amount received under a law of the United States, or of a State, that is in the nature of unemployment compensation. Neither the family leave benefits nor the medical leave benefits provided under the PFML Act are in the nature of unemployment compensation or are designed to be a substitute for unemployment benefits. Therefore, § 85 does not apply to determine the tax treatment of contributions to or benefits provided under this program.

employment, and therefore are not considered wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a).

State X must file with the IRS and furnish to Employee B a Form 1099 to report these payments of fixed or determinable income totaling $19,200 in accordance with § 6041 and § 1.6041-1.

Situation 3. Medical Leave Benefits. As in *Situation 2*, the $19,200 that State X pays to Employee B as medical leave benefits under the PFML Act provides Employee B with a clearly realized accession to wealth and is included in Employee B's Federal gross income under § 61 unless an exclusion applies. Unlike in *Situation 2*, these amounts are excluded from Employee B's gross income under § 104(a)(3) except to the extent they are attributable to Employer A's contributions that were not includible in Employee B's gross income. Amounts attributable to Employer A's contributions are included in Employee B's gross income under § 105 except as otherwise provided in that section. Medical leave benefits under the PFML Act may be paid only if time off from work is necessary because of the individual's own serious health condition, and the medical leave benefits that are paid to Employee B are, in fact, paid as a result of Employee B's own serious health condition.[12] Therefore, those medical leave benefits are received from a sickness and disability fund within the meaning of § 105(e)(2), are paid for

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[12] The IRS is of the view that, for purposes of § 104(a)(3), because of the special circumstances presented by a governmental program, including the absence of plan documents or insurance contracts, a State with a program similar to the State X PFML Act may treat its program as consisting of two separate programs, one providing solely family leave benefits and one providing solely medical leave benefits, regardless of whether both are provided under a single statute or whether both are paid from the same fund.

personal injuries or sickness, and as a result, for purposes of §§ 104 and 105, are treated as amounts received through accident or health insurance.

As determined in *Situation 1*, Employer A's mandatory contributions to the PFML Fund are properly characterized for Federal income tax purposes as State excise taxes imposed on Employer A and are therefore not included in Employee B's Federal gross income under § 61.

For purposes of §§ 104(a)(3) and 105, State X may treat its PFML program as if it were an individual insured arrangement.[13] Accordingly, because the PFML Act provides that employers must make contributions from their own funds in an amount that is no less than 40% of the standard contribution rate (1%) multiplied by each employee's weekly wages, and Employer A pays these contributions to the PFML Fund in accordance with these requirements, $7,680 ($19,200 x $416/$1,040) of Employee B's medical leave benefits is included in Employee B's gross income under § 105 except as otherwise provided in that section. The remaining $11,520 ($19,200 x $624/$1,040) is excluded from Employee B's gross income under § 104(a)(3).[14]

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[13] Thus, as under § 1.105-1(d)(1), State X may determine the portion of medical leave benefits attributable to Employer A's contributions for the taxable year by multiplying the total medical leave benefits paid to Employee B in the taxable year by the ratio of Employer A's mandatory contribution required by the State X PFML Act for the corresponding plan year to the total contributions paid by Employer A and Employee B to State X for such year.

[14] If a State PFML law does not specify the proportions of mandatory employee and employer contributions that are separately allocable to family leave benefits and to medical leave benefits, then taxpayers may assume that such mandatory contributions are allocated equally to each type of benefit. If the State PFML law specifies the rate of such contributions allocable to each type of benefit fund, then this allocation will control for Federal tax purposes.

The amount of Employee B's medical leave benefits that is includible in Federal gross income (i.e., $7,680) also constitutes wages for Federal employment tax purposes under §§ 3121(a) and 3306(b), because it is a disability leave benefit payment like those described in Rev. Rul. 72-191, and therefore is subject to the requirements of § 32.1 (and similar requirements under § 3306). It is a third-party payment (by a party that is not an agent of the employer) of sick pay, as defined in § 3402(o), and is subject to the requirements thereunder. *See generally* Notice 2015-6, 2015-5 I.R.B. 412 (describing the rules concerning responsibility for the withholding and payment of employment taxes and for reporting employment taxes and wages with respect to third-party sick pay).

Situation 4. Employer Pick-Up of Employee Contributions. The treatment of the $416 that Employer A pays from its own funds is the same as in Situation 1. However, Employer A is not permitted to deduct the $274 voluntary payment that Employer A pays to the PFML Fund from its own funds as an excise tax under § 164 because this amount is not a tax on Employer A. Because Employer A is permitted to withhold this $274 from Employee B's wages as Employee B's required contribution amount under the PFML Act, Employer A's payment of this $274 cannot be characterized as a mandatory, compulsory exaction or levy imposed on Employer A. Rather, the employer pick-up of $274 is a discharge of Employee B's mandatory contribution under the PFML Act, (*i.e.*, its State income tax liability) by Employer A in connection with the employer-employee relationship and is treated as compensation for services that is taxable as gross income to the employee. *See Old Colony Trust Co.*, 279 U.S. at 716. Accordingly,

Employer A’s payment of $274 to the PFML Fund, on behalf of Employee B, must be treated as additional compensation to Employee B under § 61.

Under State X law, the employer pick-up is excluded from wages for purposes of determining Employer A’s and Employee B’s mandatory contributions. However, this exclusion does not affect the Federal tax treatment of the employer pick-up. *See Stuart*, 317 U.S. at 161. Thus, the amount of the employer pick-up is included in Employee B’s gross income (and wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a)), and Employer A must report it on Employee B’s Form W-2 in accordance with §§ 6041 and 6051, for 2025.

As compensation paid to an employee in carrying on Employer A’s trade or business, Employer A may deduct the $274 employer pick-up as an ordinary and necessary business expense under § 162. *See* Rev. Rul. 86-14 (payments by employer of employee’s taxes are included in employee’s gross income and may be deducted by employer as ordinary and necessary business expenses under § 162). In addition, because this $274 is properly characterized as payment of Employee B’s State income taxes under the reasoning in *Situation 1*, Employee B may deduct the $274 employer pick-up in addition to the $350 withheld from Employee B’s wages as State income taxes under § 164(a)(3) in 2025. However, this deduction is available only if Employee B itemizes these State taxes on Employee B’s 2025 Federal income tax return, and only to the extent such deduction does not exceed the SALT deduction limitation provided under § 164(b)(6).

Situations 5 and 6. Family and Medical Leave Benefits with Employer Pick-Up of Employee Contributions. Because, under the reasoning in *Situation 4*, the portions of the total contributions attributable to Employer A and to Employee B are not changed as a result of Employer A's voluntary pick-up of Employee B's State income tax liability under the PFML Act, the analyses provided in *Situation* 2 and *Situation 3* would apply. Accordingly, the treatment of the $19,200 that State X pays to Employee B as family leave benefits under the PFML Act in *Situation 5,* and the treatment of the $19,200 that State X pays to Employee B as medical leave benefits under the PFML Act in *Situation 6*, are the same as in *Situation 2* and *Situation 3*, respectively.

HOLDINGS

Under the facts provided in this revenue ruling:

(1) Mandatory employee contributions that the employer withholds from the employee's wages and remits to the State pursuant to the State's PFML statute are employee payments of State income tax. Therefore, the employee may deduct these amounts under § 164(a)(3) for the taxable year in which such taxes are withheld by the employer. However, the employee may deduct these amounts only if the employee itemizes deductions in computing taxable income under § 63 and only to the extent that the employee's deduction for State income taxes is not limited by the SALT deduction limitation under § 164(b)(6). Even though these amounts are withheld from the employee's wages, they are included in the employee's gross income (and wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a)), and the

employer must report these amounts on the employee’s Form W-2 in accordance with § 6051.

(2) Mandatory employer contributions required to be paid from the employer’s own funds pursuant to the State’s PFML statute are employer payments of State excise tax. Therefore, the employer may deduct these amounts as taxes incurred in carrying on a trade or business in the taxable year they are paid or accrued by the employer under § 164(a) (flush language). Furthermore, these amounts are not included in the Federal gross income of the employee under § 61.

(3) Amounts paid to the employee by the State as family leave benefits pursuant to the State’s PFML statute are included in the Federal gross income of the employee under § 61. However, these amounts are not wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a). Nevertheless, the State must file with the IRS and furnish to the employee a Form 1099 to report payments of these amounts if they aggregate $600 or more in any taxable year in accordance with § 6041 and § 1.6041-1.

(4) Amounts paid to the employee by the State as medical leave benefits that are attributable to the employee’s contribution pursuant to the State’s PFML statute are excluded from the employee’s gross income under § 104(a)(3) and are neither wages for Federal employment tax purposes under §§ 3121(a) and 3306(b) nor treated as sick pay, as defined in § 3402(o). Amounts paid to the employee by the State as medical leave benefits that are attributable to the employer’s contribution pursuant to the State’s PFML statute are included in Employee B’s gross income under § 105 except as

otherwise provided in that section, are wages analogous to the disability leave benefit payments described in Rev. Rul. 72-191 for Federal employment tax purposes under §§ 3121(a) and 3306(b), and are third-party payments of sick pay, as defined in § 3402(o). The State must comply with the employment tax and reporting requirements that apply to such payments under § 32.1 and other guidance.

(5) If, as permitted by the State's PFML statute, the employer voluntarily pays from its own funds any part of the employee's otherwise required contribution, the amount of this employer pick-up is deductible by the employer as a business expense under § 162. Moreover, this amount is additional compensation to the employee under § 61 and included in wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a), and the employer must report it on the employee's Form W-2 in accordance with § 6051. However, the employee may deduct the employer pick-up and mandatory contributions withheld from their wages as State income tax under § 164(a)(3) to the extent permitted under §§ 63 and 164(b)(6).

(6) If, as permitted by the State's PFML statute, the employer voluntarily pays from its own funds any part of the employee's otherwise required contribution, the family leave benefit amounts attributable to this employer pick-up are included in the employee's Federal gross income under § 61, but are not wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a). Nevertheless, as with other family leave benefits, the State may be required to report the amounts in accordance with § 6041 and § 1.6041-1.

(7) If, as permitted by the State's PFML statute, the employer voluntarily pays from its own funds any part of an employee's otherwise required contribution, the medical leave benefit amounts attributable to this employer pick-up are excluded from the employee's gross income under § 104(a)(3) and are neither sick pay nor wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a).

The following tables summarize these holdings.

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 contribution	Employer may deduct the employer contribution as an excise tax under § 164.	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.	The 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 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 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.

EFFECT ON OTHER GUIDANCE

Rev. Rul. 81-194, Rev. Rul. 81-193, Rev. Rul. 81-192, and Rev. Rul. 81-191 are amplified to include the holdings in this revenue ruling that are applicable to the facts in those rulings.

Rev. Rul. 72-191, 1972-1 C.B. 45, as modified by Rev. Rul. 81-192, is further modified. Rev. Rul. 72-191 holds that employer contributions to a State nonoccupational disability fund that is treated as accident or health insurance are excluded from employees' gross incomes under § 106, and that consequently they are not wages subject to income tax withholding under § 3402. The State nonoccupational disability program addressed in Rev. Rul. 72-191 is similar in material respects to the State PFML program addressed in this ruling. Therefore, with respect to mandatory employer contributions, Rev. Rul. 72-191 is further modified to reflect holding (2) stating that these contributions are excluded from employees' gross incomes under § 61 as payments of the employer's own tax obligations, and not as employer-provided coverage under an accident or health plan under § 106. In addition, with respect to required employee contributions that are voluntarily assumed and paid by the employer, Rev. Rul. 72-191 is modified to reflect holdings (5) and (7) stating that the employer's payments are not excluded from employees' gross incomes under §§ 61 or 106, or from wages subject to income tax withholding under § 3402, and that, because they remain employee contributions, the benefit payments attributable to those amounts are excluded from the employee's gross income under § 104(a)(3).

EFFECTIVE DATE

Subject to the transition period described below, this revenue ruling is effective for payments made on or after January 1, 2025.

TRANSITION PERIOD FOR ENFORCEMENT AND ADMINISTRATION WITH RESPECT TO CALENDAR YEAR 2025

Calendar year 2025 will be regarded as a transition period for purposes of IRS enforcement and administration of the information reporting requirements and other rules described below. This transition period is intended to provide States and employers time to configure their reporting and other systems and to facilitate an orderly transition to compliance with those rules, and should be interpreted consistent with that intent. In particular:

(1) For medical leave benefits a State pays to an individual in calendar year 2025, with respect to the portion of the medical leave benefits attributable to employer contributions, (a) a State or an employer is not required to follow the income tax withholding and reporting requirements applicable to third-party sick pay, and (b) consequently, a State or employer will not be liable for any associated penalties under § 6721 for failure to file a correct information return or under § 6722 for failure to furnish a correct payee statement to the payee.

(2) For medical leave benefits a State pays to an individual in calendar year 2025, with respect to the portion of the medical leave benefits attributable to employer contributions, (a) a State or an employer is not required to comply with § 32.1 and related Code sections (as well as similar requirements under § 3306) during the calendar year; (b) a State or an employer is not required to withhold and pay associated

taxes; and (c) consequently, a State or employer will not be liable for any associated penalties.

(3) For calendar year 2025, an employer is not required to treat amounts the employer voluntarily pays from its own funds of any part of an employee's otherwise required contribution to a State paid family and medical leave program as wages for Federal employment tax purposes under §§ 3121(a), 3306(b), and 3401(a).

REQUEST FOR COMMENTS

Comments are requested on additional situations and aspects of state PFML benefit programs not addressed in this revenue ruling with respect to which the issuance of further Federal tax guidance would be helpful.

Comments should be submitted in writing on or before April 15, 2025. Consideration will be given, however, to any written comments submitted after April 15, 2025, if such consideration will not delay the issuance of guidance. The subject line for the comments should include a reference to Revenue Ruling 2025-4. All commenters are strongly encouraged to submit comments electronically. However, comments may be submitted in one of two ways: (a) Electronically via the Federal eRulemaking Portal at https://www.regulations.gov (type IRS-2025-0012 in the search field on the https://www.regulations.gov homepage to find this Revenue Ruling and submit comments); or (b) By mail to: Internal Revenue Service, CC:PA:LPD:PR (Revenue Ruling 2025-4), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, D.C., 20044. The Treasury Department and the IRS will publish for public availability any

comment submitted electronically or on paper to its public docket on https://www.regulations.gov.

DRAFTING INFORMATION

The principal author of this revenue ruling is Merrill D. Feldstein of the Office of Associate Chief Counsel (Income Tax & Accounting). However, additional personnel in the Office of Chief Counsel and at the Treasury Department participated in the development of this revenue ruling. For further information regarding the application of §§ 61 and 164 under this revenue ruling, contact Ms. Feldstein of the Office of Associate Chief Counsel (Income Tax & Accounting) at (202) 317-5100 (not a toll-free call). For further information regarding the application of §§ 104, 105, and 106 under this revenue ruling, contact Jennifer Friedman of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes) at (202) 317-5500 (not a toll-free call). For further information regarding the application of §§ 3121(a), 3306(b), and 3401(a) under this revenue ruling, contact Michael L. Gitlin, also of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes) at (202) 317-6798 (not a toll-free call).