Insight

Paid Leave and Tax Credits

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Republicans recently added a paid family leave proposal to the tax reform bill voted out of the Senate Finance Committee. The proposal closely resembles Senator Deb Fischer's Strong Families Act and would give businesses a tax credit to offset the cost of providing paid family leave. This amendment deviates significantly from other family leave proposals, and has come under swift criticism from economists and advocates on both the left and the right.

What is the proposal? Under a two-year pilot program, the federal government would provide tax credits to businesses that offer their workers paid family leave. Businesses would have to provide at least two weeks of leave and compensate their workers at a minimum of 50 percent of their regular earnings. The tax credit would range from 12.5 percent to 25 percent of the cost of each hour of paid leave, depending on how much of a worker's regular earnings the benefit replaces. The government would cover 12.5 percent of the benefit's costs if workers receive half of their regular earnings and up to 25 percent if workers receive their entire regular earnings. Businesses would only be able to apply the credit toward workers who earn below $72,000 per year. After two years, the program would expire and the General Accountability Office (GAO) would perform an analysis on the effectiveness of this approach.

This proposal is fairly intuitive and popular. Two-thirds of workers who take family leave are already paid by their employer, meaning that a federal program that simply provides paid leave benefits universally (like the FAMILY Act) is unnecessary and redundant. Moreover, the Pew Research Center found that 87 percent of Americans favor this tax credit proposal, while 62 percent favor a FAMILY Act-like proposal. Both proposals are popular, but clearly people would rather receive paid family leave from their employers rather than the federal government. And they like the idea of the government encouraging businesses to provide this benefit.

But, would this proposal actually expand access to paid family leave? The short answer: no one knows. This is a unique paid family leave proposal that has never been tried. We know that the workers without access to paid leave predominantly earn low wages and work for small businesses. So, on one hand, the proposal could help low-wage workers access the benefit and help small businesses afford it. On the other, it could simply subsidize larger businesses with higher-wage workers who already receive the benefit. Helping mitigate the latter outcome, however, the proposal would only allow businesses to apply the credit to workers earning under $72,000. This ensures that the Googles and Facebooks of the world, which already provide generous paid family leave, are not the only ones that would benefit from the proposal. Yet, it is still unclear how much of the benefit would actually expand paid leave.

The authors of the proposal seem to understand this reality, which is why the tax credits would only be available under a two-year pilot program and the GAO would be required to evaluate its outcomes. Of course, providing the benefit for only two years could limit its effectiveness. A number of businesses may hesitate to provide paid family leave, knowing they would have to take it away after two years. But, this same limitation is true of any pilot program that provides new benefits. This would, however, be a costly experiment, totaling $4.3 billion.

The proposal has come under scrutiny from those who claim it would fail to expand access to family leave. In reality, no one really knows how much it would influence businesses to provide the benefit because of the limited time frame and the novelty of the formulation. Given that the tax credits would only be available during a two-year pilot period and that we could gain a better understanding about this approach, however, this proposal has limited risk and a potentially large reward.