Employee Leave Share And Vacation Leave Donation Programs

Presentation for:
Employee Benefits Academy
October 22, 2020

Presentation by:
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Housekeeping: Questions

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- Questions during this presentation
  - We encourage questions (even though your audio lines are muted)
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About Anthony "Tony" Eppert

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- Tony practices in the areas of executive compensation and employee benefits
- Before entering private practice, Tony:
  - Served as a judicial clerk to the Hon. Richard F. Suhrheinrich of the United States Court of Appeals for the Sixth Circuit
  - Obtained his LL.M. (Taxation) from New York University
  - Obtained his J.D. (Tax Concentration) from Michigan State University College of Law
    - Editor-in-Chief, Journal of Medicine and Law
    - President, Tax and Estate Planning Society

Upcoming 2020 & 2021 Webinars

- **Upcoming 2020 webinars**:
  - **October 22**: Employee Leave Share and Vacation Leave Donation Programs
  - **November 19**: Year-End Benefit Plan Requirements/End of Year Benefits “To Do” List Benefits
  - **December 17**: Benefits Year in Review and a Look Ahead to the Upcoming Year
- **2021 webinars**:
  - **January 28**: Cafeteria Plan Mid-Year Election Change Rules
  - **February 25**: Deferred Compensation Arrangements - Key 409A Issues
  - **March 25**: Legal Updates on DOL Guidance for 401k Investments and Fiduciary Rule
  - **April 22**: ERISA Fiduciary Litigation Update
  - **May 20**: Public Company ESOP Issues
  - **June 24**: Key Issues for HSAs, HRAs and FSAs
  - **July 22**: Employment and Benefits Issues in M&A Transactions
  - **August 26**: Basics and Update on IRS and DOL Correction Programs
  - **September 23**: Self-Directed IRAs and investments relating to the same
  - **October 28**: Navigating controlled group and affiliated service group rules
  - **November 18**: Year-End Benefit Plan Requirements/End of Year Benefits "To Do" List
  - **December 16**: Benefits Year in Review and a Look Ahead to the Upcoming Year
- Sign up here: Employee Benefits Academy Webinar Series - Subscribe

Purpose of this Presentation

- The purpose of this presentation is to discuss how employers can help employees who are negatively impacted due to federally declared disasters

- To that end, this presentation covers:
  - PTO donation,
  - Foregone leave followed by charitable donation,
  - Section 139 payments to employees,
  - Donor-advised funds, and
  - 501(c)(3) employee relief fund

PTO Donation

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- The concept of PTO donation is also known as leave donation or leave sharing programs
- Typically used in conjunction with natural disasters, an employer could develop a PTO (paid time off) donation program whereby employees may donate all or some of their accrued but unused PTO to a pool for the benefit of other employees who need time off to cope with adverse effects of a natural disaster
- Elements of a typical PTO donation program resulting from a natural disaster include:
  - Employee makes a irrevocable 1x donation of certain accrued but unused PTO hours
  - Typically there is both a minimum and maximum number of PTO hours that may be donated
  - The donated PTO hours are deposited into a "bank" (for lack of a better term)
  - The PTO donation is documented pursuant to a written donation form, within which the donor employee represents that he or she will not claim an expense, charitable contribution, or loss deduction with respect to such donated PTO
  - Employees who are "adversely affected" by the natural disaster (*i.e.*, such disaster caused a severe hardship to the employee or his/her family such that the employee is required to be absent from work) may request PTO from the "bank"
  - Eligibility to receive donated PTO time is typically governed by a committee
  - The requesting employee submits a request for donated PTO pursuant to form

PTO Donation

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- [Continued from prior slide]:
  - There is a maximum limit on the number of PTO hours that may be requested
  - No “earmarking” by donor employees permitted
  - Donated hours are processed at the recipient’s rate of pay for purposes of FICA and FUTA
  - There is no reversion to the donor employee, except that, if at the end of the designated period set by the employer to respond to the natural disaster, there remains unused donated PTO, then:
    - The donor employee will receive a restoration of some of his/her donated PTO
    - Such restoration will be equal to the ratio that his/her donated PTO bears to the total amount of donated PTO pursuant to the program

PTO Donation

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- Tax law
  - Generally, due to the “assignment of income doctrine,” an employee is taxed on PTO earned if he/she has a choice between using the PTO or donating it
  - However, two exceptions could apply where the donor is not taxed on the donated PTO
    - Medical Emergency Exception is defined as a “medical condition of the employee or a family member that will require the prolonged/extended absence of the employee from duty and will result in a substantial loss of income to the employee due to the exhaustion of all paid leave available, apart from the leave-sharing plan.” *See* PLR 200720017; Rev. Rul. 90-29.
    - Major Disaster Exception is defined as a disaster declared by the President of the U.S. pursuant to certain Acts. *See* Notice 2006-59
  - The following are the minimum design elements of the Medical Emergency Exception:
    - The program must be restricted to “medical emergencies”
    - The recipient employee must be required to exhaust all forms of paid leave prior to receiving benefits under the program
    - Recipient employees should not receive leave greater than their normal rate of compensation (otherwise the program could be deemed as other than a “payroll practice” and subject to ERISA)
    - An administrative approval process should be implemented
  - The prior two slides essentially set forth the requirements of the Major Disaster Exception under Notice 2006-59

PTO Donation

- Consider budget concerns
  - A PTO donation program could artificially increase the use of PTO that would have otherwise been forfeited at the end of the year (*e.g.*, payroll expenses)
  - What if lower-paid employees make up a larger percentage of the donor and higher-paid employees make up a larger percentage of the recipients?

COVID-19 Foregone Leave/Charitable Donation Program

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- Pursuant to Notice 2020-46, an employer could design a program whereby an electing employee would forego certain PTO, and in exchange, the employer would take the cash equivalent and donate such to a charitable organization described in Section 170(c) that is chosen by the donor employee
  - The charity must provide relief for COVID-19 victims
  - The charity must make payments prior to January 1, 2021
- The foregone leave is not taxable income to the donor employee if the cash contribution by the employer is to a Section 170(c) qualified charity
- As a result of the cash contribution, the employer is entitled to a charitable deduction under Section 170 or a business deduction under Section 162
  - The donor employee is not entitled to a charitable deduction

Section 139 Payments to Employees

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- Section 139 of the Code allows employers to make qualified disaster relief payments to (or for the benefit of) its employees who are impacted by a federally declared disaster
  - If Section 139 applies, then the payment by the employer to the employee would not be considered gross income to the employee for federal income tax purposes (though state tax may apply)
  - The payment may be used by the recipient employee for:
    - Funeral expenses
    - Living expenses
    - Personal expenses such as hospital bills
    - Family expenses
    - Repair of primary residence or its contents
  - The employer has no substantiation requirements
  - There are no limits and typical non-discrimination rules do not apply
  - Section 139 payments are deductible by the employer
  - On March 13, 2020, the COVID-19 pandemic was declared by the President to be a qualified disaster for purposes of Section 139
- With respect to COVID-19, the types of expenses that can be reimbursed by the employer under Section 139 include (if expense incurred due to COVID):
  - Costs of a home office
  - Dependent care expenses
  - COVID-19 medical expenses not otherwise covered by insurance

Donor-Advised Fund within a Public Charity

- In the context of a federally declared disaster, an employer could donate monies to a donor-advised fund, maintain privileges over the distribution of such monies, and ensure such monies are used for the benefit of its employees who were affected by such disaster

- Thoughts to consider include:
  - Selection of employee recipients must be made upon an objective determination of financial need;
  - Typically, a selection committee will make the foregoing determination; and
  - The fund should maintain records that establish the recipient's financial need

501(c)(3) Employee Relief Fund

- If the employer desires that employees who are unaffected by the qualified disaster would have the ability to contribute monies, then the employer could establish a 501(c)(3) charity for such purpose

- In terms of taxation:
  - The donor would be entitled to a deduction
  - The employer would have no tax liability
  - The recipient would have no tax liability

- Burdens include:
  - A corporate entity must be established
  - An application to the IRS must be filed seeking tax-exempt status under 501(c)(3)
  - A conflict of interest policy should be adopted
  - A committee to run the program should be organized
  - The committee must establish objective criteria to assess financial hardship/need