American Payroll Association

Government Relations • Washington, DC

Mr. Timothy F. Geithner
Secretary of the Treasury
Department of the Treasury
1500 Pennsylvania Avenue, NW
3330 MT
Washington, DC 20220

Mr. Mark Mazur
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Avenue, NW
3120 MT
Washington, DC 20220
E-Mail: mark.mazur@treasury.gov

Mr. George Bostick
Benefits Tax Counsel
1500 Pennsylvania Avenue, NW
3050 MT
Washington, DC 20220
E-mail: george.bostick@treasury.gov

Mr. Steven T. Miller
Acting IRS Commissioner
1111 Constitution Avenue
3000 IR
Washington, DC 20224

Michael J. Montemurro
Chief, Branch 4 (IT&A)
1111 Constitution Avenue, NW
4243 IR
Washington, DC 20224
E-Mail:
michael.j.montemurro@irscounsel.treas.gov

Mr. Sheldon A. Iskow
Attorney, Branch 4 (IT&A)
1111 Constitution Avenue, NW
4229 IR
Washington, DC 20224
E-mail: sheldon.a.iskow@irscounsel.treas.gov

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Re: Proposed Reinstatement of Employee Leave-Reduction Rules, to Assist Victims of Hurricane Sandy

Dear Sirs:

The American Payroll Association ("APA") is writing to request the reinstatement of the special temporary rules allowing employees across the United States to elect (through payroll deductions) to donate their vacation and sick pay to help provide financial assistance to victims of Hurricane Sandy.

The Internal Revenue Service has twice before provided such payroll reduction donation relief, in Notice 2001-69, 2001-2 C.B. 441 (applicable after 9/11), and Notice 2005-68, 2005-2 C.B 622 (applicable after Hurricane Katrina). We believe similar relief is warranted now, and should be reinstated immediately (and expanded), to encourage salary reduction contributions before year-end, and continuing through 2013.

The APA is the country’s leading private sector advocate for payroll and information reporting issues. The APA is a nonprofit association representing 21,000 payroll professionals, and for the major payroll service providers in the United States who, in turn, process payrolls for an additional 1.5 million employers. The employers for whom APA members process payrolls are diverse in terms of business size, location, and industry. As payroll specialists, APA’s members must determine proper employment tax withholding, prepare and file accurate information returns and statements, correct (when necessary) such information returns and statements, calculate and deposit taxes, and maintain all necessary payroll records.

APA members are concerned about providing much-needed disaster-assistance relief in the most efficient manner possible.

Notice 2001-69 (as modified and superseded by Notice 2003-1, 2003-1 C.B. 257), was the helpful ruling that applied for 15 months after 9/11 to facilitate employee donations to other employees. Notice 2005-68 provided similar relief after Hurricane Katrina, which extended from September 2005 throughout 2006. Under these Notices, employers were permitted to adopt leave-based donation programs under which employees could forgo vacation, sick, or personal leave in exchange for employer contributions to charitable organizations described in Section 170(c) of the Internal Revenue Code. The Notices encouraged employee donations by conferring tax advantages without requiring employees to claim deductions on their personal returns.

If this donation relief is reinstated to assist the victims of Hurricane Sandy who live in the Federally declared disaster areas in New York, New Jersey and Connecticut, the following tax benefits would apply (all of which operate to encourage and facilitate donations to the needy victims and their families):

- Any employee donating leave would be given relief from both income taxes and the employee share of FICA taxes. **This provides an even greater tax incentive for employees to donate than exists under normal charitable donations, where the employee may claim an income tax deduction on his or her Form 1040, but is still subject to FICA taxes.** Under any such donation-relief Notice, the employee would not claim any income-tax deduction, but instead could elect to transfer salary back to the employer, or a designated charity (like the Red Cross), and would not be taxed for either income or FICA tax purposes on the transferred monies.

- The amount of FICA taxes saved would vary, depending on the employee’s income. Employees earning under $110,100 in 2012 will save FICA taxes at a rate of 5.65%; employees earning more than that amount will save the Medicare portion of FICA taxes at a rate of 1.45%. When donations continue, in 2013, Employees earning under $113,700 in 2013 will save FICA taxes at a rate of 7.65%; employees earning more than that amount will save the Medicare portion of FICA taxes - which in 2013 will be imposed at a rate of 1.45% for most employees, and at a rate of 2.35% on any employee’s wages exceeding $200,000.

- If an employee is paid wages and claims an offsetting income tax deduction, that deduction is subject to the 2% of AGI floor under Internal Revenue Code Section 67. But under the IRS's leave-donation relief Notices, this deduction minimum is avoided, enabling employees to donate more funds for relief efforts.

- The employer is allowed to claim a business expense deduction under Code Section 162 instead of a charitable contribution deduction (which might be limited, if the employer has already made charitable contributions in that year up to the Code's limitations on charitable contribution deductions).

The addition of Section 139 to the Internal Revenue Code in 2001 (after Notice 2001-69 was issued) has given the Treasury Department greater flexibility to provide tax relief to victims of Federally declared "disaster areas." Code Section 139 excludes from income all "qualified disaster relief payments." Thus, technically it would no longer be necessary for the IRS to require employees to designate specific charities as recipients of their funds; rather, employees ought to be allowed simply to assign wages back to their employer's "Hurricane Sandy Relief Fund," which would not need to be established as a foundation. The employer could then disburse the funds as excludable qualified disaster relief payments under Code Section 139, on a tax-free basis, to help reimburse employees afflicted by Hurricane Sandy, to help repair and rebuild their homes, and to help pay for their personal, family, living, or funeral expenses incurred as a result of this qualified disaster.[1]

It also seems unnecessary to require employees to make their contributions by assigning leave days, as required in Notices 2001-69 and 2005-68. Employees are already permitted to "purchase" leave days from their employers with pre-tax dollars through a cafeteria plan under Code Section 125. Rather than requiring this formalistic procedure, it would be much more efficient for the IRS to allow employers to avoid those additional steps and permit employees to simply assign designated amounts of their wages, rather than "leave days," for Hurricane Sandy Relief.

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[1] After the expiration of the relief provided by Notice 2005-68, the IRS released Notice 2006-59; 2006-2 C.B. 60, which continues to permit employees to assign accrued leave (not exceeding the amount of leave that an employee normally accrues) to other employees affected by a major disaster, but which provides substantially limited tax benefits, compared to the prior years' Notices. Such a plan does not allow the leave donors to assign leave to specific recipients, required the employer to select the recipients, and to make reasonable determinations as to how much leave each recipient may receive. Notice 2006-59 also requires that the leave recipient must use the leave as leave, with the payments treated as wages subject to income taxes, income tax withholding, and FICA taxes. No conversion of the leave donations into cash or tax-free disaster relief under Code Section 139 is possible. Any leave not used as such by the employees affected by the disaster must be returned to the leave donors, in proportion to the amount of leave that was donated by all the donors collectively.

We appreciate the Administration's prompt and efficient efforts to find as many ways as possible to facilitate the provision of aid to the victims of Hurricane Sandy. We believe that reinstating the disaster-assistance tax relief in the manner described above will go a long way toward promoting an easy and efficient method for employees and employers to set up donation programs through salary reduction.

Sincerely yours,

Brian O'Laughlin, Esq.
Manager of Government Relations
American Payroll Association
202-232-6888 (p)
bolaughlin@americanpayroll.org