COVID-19: Employer Assistance Opportunities

On March 13, 2020 the President declared a national emergency (qualified disaster) under the Robert T. Stafford Disaster Relief and Emergency Assistance Act due to the COVID-19 outbreak. With this declaration, various avenues for tax-advantaged financial assistance beyond paid leave are opened to employers who have employees affected by the virus. Those avenues are discussed below along with some other opportunities to help.

Coronavirus Related Retirement Plan Distributions

- Pursuant to the recently enacted CARES Act, plan sponsors can immediately change their plans to allow for a Coronavirus Related Distribution (CRD). The 10% early withdrawal penalty is waived for such a distribution between January 1, 2020 and December 31, 2020 for an amount not to exceed $100,000 in the aggregate.
- The waiver only applies to an individual (1) who is diagnosed with COVID-19, (2) whose spouse or dependent is diagnosed with COVID-19, or (3) who experiences adverse financial consequences as a result of being quarantined, being furloughed or laid off or having work hours reduced due to such virus or disease, being unable to work due to lack of child care due to such virus or disease, closing or reducing hours of a business owned or operated by the individual due to such virus or disease.
- It will be up to the individual (not the plan sponsor) to self-certify that he/she meets the requirements for a CRD.
- A CRD will not be subject to tax withholding. The individual will recognize the income for federal tax purposes of a CRD ratably over a 3-year period beginning with the year of distribution, instead of all in the year of distribution. The individual may opt out of this 3-year treatment and recognize the income all in the year of distribution. Amounts taken as a CRD can also be repaid (rolled over) to an eligible retirement plan at any time over the 3-year period commencing on the day after the CRD was received. There is no requirement that repayment be made at one-time, rather repayment can be spread out over the entire 3-year period through one or more contributions. It is not clear how such repayments will be treated where income was recognized on the distribution in an earlier year (further guidance will be needed). It is also not clear whether a plan sponsor's acceptance of a repayment (rollover) is optional.

- If the change is enacted, an amendment must be adopted. The deadline to adopt the amendment is December 31, 2022 (for a non-calendar year plan, the end of the plan year that starts in 2022).

IRC §139 Qualified Disaster Relief Payments (QDRPs)

- Generally, any payments an employee receives from his/her employer are considered taxable income. However, IRC §139 provides an exception to this general rule for QDRPs in times when the federal government declares a qualified disaster. Employers are then permitted to provide qualified disaster relief payments to employees to reimburse or pay reasonable and necessary personal, family, living, or funeral expenses incurred as a result. These payments would be deductible by the employer. There is no limit as to the amount of such payments.
- COVID-19 related expenses eligible for reimbursement may include: medical expenses (e.g., co-pays, deductibles, vitamins, and supplements), health-related expenses that are not medical expenses (e.g., over-the-counter medications, hand sanitizers), increased expenses associated with being quarantined at home (e.g., increased utilities), expenses associated with setting up or maintaining a home office (e.g., enhanced internet connections, computer monitors, laptops, printers, office supplies), child care expenses due to school closings, and housing for additional family members, (e.g., transportation and living expenses for college students returning home including duplicative meal expenses).
- Employees are not required to account for or substantiate qualifying expenses, provided that the amount of the payments can be reasonably expected to be commensurate with the expenses incurred.
- This tax-free assistance cannot cover expenses that would otherwise be reimbursed by insurance, income replacement for lost wages, and/or assistance for hardships that aren't related to the declared disaster.
- QDRPs do not require a written plan document, are not subject to discrimination testing, are not subject to payroll taxes and are not subject to W-2 reporting.
- As the breadth and duration of this virus is unknown, unlike hurricanes where the physical disaster expenses are easily identifiable, the exact application of this provision in the current environment remains uncertain.

Reimbursement of Home Office Expenses

- Employers may wish to reimburse employees for expenses related to their home offices as working from home is likely considered "for the convenience of the employer" in most circumstances. Examples, of such expenses includes internet service, phone service, cleaning supplies, office supplies, etc.
- It is important to note that employees cannot otherwise currently take a deduction for unreimbursed employee business expenses since miscellaneous itemized deductions have been suspended through 2025.
- Outside of qualifying under §139 as described above, whether these reimbursements will be considered as qualified working condition fringe benefits under IRC §132(a)(3) and therefore not income taxable, needs further IRS clarification.

Special Bonus/Cash Payment

- Employers may wish to provide a one-time cash bonus to their employees without structuring the payments to meet QDRP guidelines. This allows the employee more flexibility as to how the funds are used.
- These payments would be taxable compensation to the employee; however, employers may provide a gross up to alleviate the tax consequences.
- As an illustration, one company is providing US employees who make $60,000 or less a $1,000 special bonus while another is providing $600 to employees who make less than $100,000 and worked for the full 2019 calendar year.

Company Loans

- Pursuant to IRC §7872, an employer is permitted to make an interest-free loan to an employee of up to $10,000 without having to treat the foregone interest as compensation to the employee. In addition, if the employee currently has received a loan in excess of $10,000 from his or her employer, the employer can still make an additional loan to that employee as long as the rate of interest is at least equal to minimum rate established under the provisions of the Tax Code. For short-term loans (less than 3 years) originated in April 2020, the rate is 0.91%. This rate is significantly lower than commercial loan rates that might otherwise be available to employees looking for ways to manage through these difficult economic times.
- Alternatively, bona fide loans by employers to employees will generally not result in taxable income unless forgiven. The IRS looks to see if there is a legitimate debtor creditor relationship, including repayment of interest (at least equal to the applicable federal rate) and principle, sufficient collateral, and terms to which a legitimate bank would require. An employee loan with an expectation of employer forgiveness from the start can be deemed upfront compensation.

Student Loan Assistance

- Under the CARES Act, employers are allowed to treat certain reimbursements made before January 1, 2021 of student loan principal and interest as being paid on a pre-tax basis (subject to limits).
- For an employer that sponsors an educational assistance program, benefits provided by the employer to the employee can currently be excluded from income up to $5,250 per year. Under the CARES Act, the definition of amounts that can be reimbursed on a pre-tax basis is expanded to include the payment of principal and interest on student debt, but the total education assistance and student loan benefits will still be limited to $5,250. Payments can be made by the employer directly to the lender or to the employee. The employer will need to amend the plan to add student loan payments as an eligible expense.
- Also note that principal and interest payments on any student loans owned by the federal government can be deferred through September 30, 2020 without any penalty to the borrower. Interest will not accrue on the balance during this period.

Employer-Sponsored Charitable Relief Fund

- Employers may want to consider establishing a charitable Employee Relief Fund to provide additional funds to employees in need due to COVID-19. If structured properly, payments to employees from the fund will not be taxable income and will have no W-2 reporting requirements.
- This could be used as an alternative or in addition to §139 QDRPs, and could be funded with tax-deductible charitable contributions made by the employer and others that want to help. These funds can make a broader array of tax-free distributions to employees than those payments allowable under a §139 QDRP.
- Since these types of funds are established as a charitable fund at a 501(c)(3) tax-exempt organization, payments from an Employee Relief Fund must comply with various IRS requirements. This will include having a significantly large charitable class, requiring the selection of the recipients on an objective determination of need, making sure any potential benefit to the employer is incidental, and the use of an independent selection committee to select recipients.
- An employer could add a new charitable organization and apply for tax-exempt status with the IRS, but it is often more efficient to use existing charities to operate the fund. Another option is an employer-sponsored private foundation. Generally, an employer-sponsored private foundation cannot disburse funds directly to an employee without a significant penalty to the foundation. Since COVID-19 is considered a qualified disaster under §139 of the Internal Revenue Code, an employer-sponsored private foundation can be used to provide direct aid to employees without penalty and on a tax-free basis to the employee.
- An Employer-sponsored Donor Advised Fund (DAF) can be established quickly with an existing foundation or charity. They may accept charitable contributions from anyone, including the employer, employees and the general public. While DAFs are generally prohibited from making distributions to individuals, employer-sponsored DAFs which serve the single identified purpose of providing relief from a qualified disaster are permitted to make tax-free payments to employees and their family members who have been affected. Similar to the charitable vehicles previously noted, a DAF must also comply with IRS requirements including that recipients of the financial assistance must be selected based on need and any potential benefit to the employer must be incidental.

Leave-Sharing and PTO Arrangements

- Leave-sharing arrangements allow employees to donate accrued leave to other employees. Generally, the leave is taxable to the donor employee; however, the IRS provides two exceptions in situations where the donation is made in connection with either a “major disaster” or a “medical emergency”. In either of these situations, it is the leave recipient and not the leave donor who will recognize the payment as taxable compensation. Leave-sharing programs must be properly documented in writing.
- IRS Notice 2006-59 permits employees to donate accrued leave to an employer-sponsored leave bank for use by their coworkers who have been adversely affected by a major disaster declared by the President. For this provision to apply, it has to be more than an emergency (qualified disaster) declaration under the Stafford Act. There must be an actual declaration of a major disaster in the state or region where the employee resides. To date, the President has declared a major disaster in California, New York, Texas, Florida, and several other states.

The full list of states falling under a major disaster declaration can be found on the FEMA website (https://www.fema.gov/disasters). An employee is considered to be adversely affected by a major disaster if the event has caused severe hardship to him/her or a family member that requires the employee to be absent from work.

- IRS guidance in Revenue Ruling 90-29 permits employees to donate leave to an employer-sponsored leave bank for use by other employees affected by a medical emergency. To qualify for the favorable tax treatment discussed above, the plan must be available to "eligible recipients" only and the recipient employee is required to exhaust all other forms of paid leave (e.g., paid time off, sick leave) before using the leave bank. Eligible leave recipients include any employee or family member with a medical condition that requires a prolonged absence of the employee from work and results in a substantial loss of income. Employees requesting the additional leave are required to submit a written application describing the medical emergency to the employer for approval. The diagnosis of COVID-19 is not necessarily an automatic qualifier, the ultimate decision will depend upon the facts and circumstances of each case.
- Employers may also want to consider expanding their current sick time policies to include caregiving related to COVID-19.

Health Care/Dependent Care

- Employers may want to consider paying all or part of self-insured health insurance premiums during a temporary layoff/furlough (if fully insured, subject to insurer's contract). Employers must ensure that the rules outlined in the plan document and SPD are followed. Failure to administer a plan in accordance with the written terms of the plan and the Internal Revenue Code can result in the loss of the benefits' pretax status. Also, employers should determine whether there are any §125 cafeteria plan issues with stopping or reducing employee contributions and how to effectively transition back to normal cost-sharing. Employers can also consider whether they want to allow non-enrolled employees to special enroll given the same considerations as discussed above.
- Employers may want to consider permitting employees to make changes to their cafeteria plan elections due to a change in circumstance resulting from COVID-19. Under a §125 cafeteria plan, an employee is permitted to revoke elections made before the beginning of the plan year only under special circumstances, which include a change in the employment status of the employee (or the employee's spouse or dependents) or the offering of a special election period under the plan. The change in the election must also be consistent with the change in status. For example, when an employee's eligibility for or cost of coverage under the group health plan changes because the employee experiences a reduction in hours as a consequence of COVID-19, the employer must allow the employee to make a change in his or her §125 cafeteria plan elections. In addition, if an employee is on an FMLA leave of absence due to COVID-19, whether because of their own illness or to care for a family member, the employer must allow the employee to revoke their coverage under the employer's group health plans, if desired.
- Employees may also experience a change in the cost of dependent care – either a decrease in cost due to the closing of daycare facilities or an increase in cost due to the need to arrange alternative childcare following a school closing. Such change in dependent care cost is a valid mid-year election change event that would require employers to allow an

employee to make a corresponding change to their dependent care flexible spending account election – to either stop/decrease or start/increase contributions to the employer's dependent care flexible spending account, as applicable.

Adjustments to State Withholding

- Where an employee resides in a different state (resident state) from where he/she works (nonresident state), a work at home arrangement mandated by the employer can create an additional tax liability to the resident state and a lesser tax allocation to the nonresident state.
- Adjustments to state withholding to account for just such a situation can be very helpful (and in some situations mandated by state law) so as to avoid a surprise liability come the 2020 tax season. In limited situations, we have seen employers make an employee whole for an increase in liability due to the change. Additionally, providing proper employee education on how the computation of state tax liability, credits and reciprocity agreements work when dealing with a multi-state situation is critical.

Employee Purchase Program

- An employee purchase program provides employees access to products and services on an interest-free basis through payroll deduction (typically through a provided website). As a voluntary benefit, employers can provide it as a low- or no-cost addition. Such a plan can be a relief to employees that are in financial trouble and need to make a major essential purchase such as a computer, appliances, electronics, furniture, baby products, automotive services, etc. Various 3rd party vendors are available to administer such a program.

Besides the opportunities described here, employers should take this time to highlight and explain the features/advantages of voluntary benefits likely already being offered such as short-term disability, employee assistance programs, wellness programs, hospital indemnity insurance, critical illness insurance, life insurance, etc.

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