

Hurricane Recovery Client Alert: Establishing a Charitable Leave Donation Program

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Tips on setting up a pooled fund of employee leave by giving employees the option of donating leave that can be converted into cash contributions to charities assisting the victims of Hurricane Harvey.

As millions of families in Texas and Louisiana deal with the devastating effects of Hurricane Harvey, individuals and businesses around the country are actively seeking opportunities to help. In response to this crisis, the IRS released Notice 2017-48 on September 5 to significantly expand the tax benefits of certain charitable cash contributions for hurricane relief. More specifically, the IRS guidance encourages employers to establish charitable leave donation programs to provide assistance to those dealing with the aftermath of Hurricane Harvey.

This addendum to our [Hurricane Harvey Client Alert: How Employers and Employees Can Help Those in Need](#) explains the IRS guidance in more detail and provides background for employers that are considering establishing such programs to provide immediate disaster assistance relief to the victims of Hurricane Harvey. We expect the IRS to issue similar guidance in response to Hurricane Irma.

Sample Form and FAQs

Although charitable leave donation programs are easy to establish and administer, few employers have done so due to a lack of knowledge of the programs and/or because such programs only come into relevance in conjunction with a catastrophic event such as Hurricane Harvey.

While we wish that these programs were never necessary, an [example election form](#) and list of [Frequently Asked Questions](#) are linked for reference to aid employers that may be considering setting one up, as well as for employees who may have questions about donating leave to such a program. The election form is an illustrative example (for information purposes only) but can be revised as necessary to fit an employer's specific needs in consultation with its own tax and legal advisors.

What is a Charitable Leave Donation Program?

A charitable leave donation program is a pooled fund of employee leave. The principle objective of

the program is to encourage charitable cash contributions to relief efforts in the wake of catastrophic events like Hurricane Harvey by providing employees with the option of donating their accrued-but-unused leave.

Many employees do not have readily expendable resources to donate to relief efforts when disasters occur, and in some cases employees may wish to donate more than the cash they have already donated. A charitable leave donation program helps in both respects by allowing employees to convert unused vacation, sick, or personal leave into cash contributions that the employer transfers to charitable organizations assisting victims.

The program offers employees a simple method of leave donation. Employees can make charitable donations of leave to the program, and employers can either designate certain charitable organizations to receive the cash value of the donations or allow the employees to pick one or more specific charitable recipients from a list prepared by the employer. The recipients should be charitable organizations—including national, regional, and faith-based organizations—that are assisting hurricane victims.

How Does It Work?

In establishing a charitable leave donation program, employers are given latitude to design a program that fits within the employer's particular needs, circumstances, and policies. At a basic level, the employer must decide who is eligible to participate in the program and what types of leave may be donated. Many employers will allow all employees who are eligible to accrue leave to participate, and will permit any type of leave (including sick leave) to be donated. The employer must also determine in what increments leave can be donated, (i.e., hours, days, weeks).

The employer establishes an open enrollment period after making these basic decisions. During this enrollment period, employees are able to file an election form with the employer to donate accrued leave or to pledge leave that will be accrued in the future.

Once the employee elects an amount of leave either to donate at one time or to pledge over time, the employer will contribute directly to the charitable organization a cash amount equal to the gross amount of the employee's donated leave. The employer then reduces the employee's leave balance by a corresponding amount. For example, if the employee is paid \$20 per hour and donates eight hours of personal leave, the employer will make a cash donation of \$160 to the charitable organization and reduce the employee's leave balance by eight hours.

What Is the Favorable Tax Impact of Participating in the Program?

The IRS has extended favorable tax treatment to both employers and employees that override traditional tax principles of constructive receipt and assignment of income for contributions made prior to January 1, 2019. In particular, the IRS will not assert that the employee's election to donate accrued leave triggers constructive receipt of employee wages. In plain English, employees can effectively donate in a more tax-efficient manner than if they had claimed a charitable deduction because the charitable leave donations are effectively pretax donations. This pretax treatment means that the donations of accrued leave

- are exempt from income taxes,
- are exempt from Federal Insurance Contributions Act (FICA) taxes,

- are exempt from alternative minimum tax (AMT), and
- avoid the limitations placed on charitable contributions by those employees who do not file itemized tax returns.

This is a favorable tax tradeoff that more than offsets the fact that the employer, not the employee, is the taxpayer that claims the deduction for the contributions. And the charitable organizations aiding the victims receive a larger cash donation due to the effects of this pretax treatment.

As noted above, employers receive favorable tax treatment from these programs. Although the employees cannot claim a charitable contribution deduction, employers are permitted to elect to deduct the cash payments either as charitable contributions (up to the applicable limitations) or as business expenses. In addition, the employer reduces its FICA tax liability because the donations, as compared to the leave payments, are exempt from FICA taxes. It is important to note that if the employee donating leave cannot carry over unused leave or receive a “cash-out” for the unused leave, then the employer may bear the financial burden of making the contributions. Such employers can require that the employees donate from otherwise nonforfeitable leave or limit the amount of forfeitable leave that can be donated.

This favorable tax treatment is permitted in IRS Notice 2017-48. As with only a small number of previous major disasters (e.g., 9-11, Hurricane Katrina, Hurricane Sandy), the IRS notice adopts a nonenforcement position. In the notice, the IRS confirms that any cash payments made by the employer that represent the donated leave will not be considered gross income or wages to the employee if the payments are made to certain charitable organizations described in section 170(c) of the Internal Revenue Code. The donations must be made for the relief of victims of Hurricane Harvey.

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