

# SNURE LAW OFFICE, PSC

A Professional Services Corporation

**Clark B. Snure**  
clark@snurelaw.com

**Brian K. Snure**  
brian@snurelaw.com

Of counsel  
Thomas G. Burke  
Joseph F. Quinn

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## MEMORANDUM

To: Washington State Fire Districts and Regional Fire Authorities

From: Brian Snure and Joseph F. Quinn

Re: Volunteer Compensation

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The following memorandum provides an overview of the appropriate method for managing and reporting volunteer compensation (expense reimbursements) for fire protection districts and regional fire authorities collectively referred to as “fire departments.” Payments to volunteer firefighters must be analyzed under two separate and somewhat contradictory legal frameworks: (1) income tax and other laws interpreted by the IRS, which are different from (2) FLSA and other federal or state laws.

**Issue 1:** What are the rules for providing compensation to volunteers without turning the volunteers into employees for minimum wage and overtime purposes? This issue requires consideration of the application of the minimum wage and overtime requirements imposed by the United States Department of Labor under the Fair Labor Standards Act “FLSA” and the Washington State Department of Labor and Industries of the Washington State Minimum Wage Act “MWA”. This issue is addressed in part 1 of this memorandum.

**Issue 2:** What requirements must a fire department comply with in reporting the compensation received by a volunteer, pursuant to various federal and state statutes, rules and regulations? This issue requires a consideration of the rules of the Internal Revenue Service, Social Security Administration and various state taxing departments such as Labor and Industries and the Employment Security Department. This issue is addressed in part 2 of this Memorandum.

### PART I – FLSA/MWA VOLUNTEER EXEMPTION

The Fair Labor Standards Act excludes **bona fide** volunteers from coverage of the Act. The MWA also recognizes a volunteer exemption and will generally follow the guidance created by the FLSA.

**Creation of Volunteer Status.** Sections 553.101 and 553.104 of the regulations define the term volunteer. The key elements in a volunteer relationship under the FLSA and MWA include the willing provision of services without promise, expectation or receipt of compensation. Section 553.101 provides in part as follows:

*(a) An individual who performs hours of service for a public agency for civic, charitable, or humanitarian reasons, **without promise, expectation or receipt of compensation for services rendered**, is considered to be a volunteer during such hours....*

*(b) Congress did not intend to discourage or impede volunteer activities undertaken for civic, charitable, or humanitarian purposes, but expressed its wish to prevent any manipulation or abuse of minimum wage or overtime requirements through coercion or undue pressure upon individuals to ``volunteer'' their services.*

*(c) Individuals shall be considered volunteers only where their services are offered freely and without pressure or coercion, direct or implied, from an employer.*

*(d) An individual shall not be considered a volunteer if the individual is otherwise employed by the same public agency to perform the same type of services as those for which the individual proposes to volunteer. (emphasis added)*

**Payments to Volunteers.** Under sections 553.104 and 553.106 of the regulations, individuals who voluntarily agree to perform fire protection activities on a part-time basis as a public service are not considered to be employees of the fire department even though the fire department may provide benefits including courses of training paid for by the fire department; reimbursement for approximate out-of-pocket expenses incurred incidental to providing the service, i.e., uniforms, replacement of clothing damaged while responding to a call; the fire department's premiums for the Volunteer Fire Fighters' Relief and Pension System; and insurance benefits.

In section 553.106 of the regulations, the Department of Labor has provided authorization for these limited payments to volunteers. The section provides substantially as follows:

*"Volunteers may be paid expenses, reasonable benefits, a nominal fee, or any combination thereof, for their service without losing their status as volunteers.*

*Individuals do not lose their volunteer status if they receive a nominal fee from a public agency. A nominal fee is not a substitute for compensation and must not be tied to productivity. However, this does not preclude the payment of a nominal amount on a 'per call' or similar basis to volunteer firefighters. The following factors will be among those examined in determining whether a given amount is*

*nominal: The distance traveled and the time and effort expended by the volunteer; whether the volunteer has agreed to be available around-the-clock or only during certain specified time periods; and whether the volunteer provides services as needed or throughout the year. An individual who volunteers to provide periodic services on a year-round basis may receive a nominal monthly or annual stipend or fee without losing volunteer status.*

*Whether the furnishing of expenses, benefits, or fees would result in individuals' losing their status as volunteers under the FLSA can only be determined by examining the total amount of payments made (expenses, benefits, fees) in the context of the economic realities of the particular situation."*

This section has resulted in several acceptable methods of making limited payments to volunteers. The following sections discuss each of the approaches used by fire departments.

**Expense Reimbursement System.** A fire department may attempt to reimburse the actual expenses incurred by volunteers. Under an accountable plan, each volunteer would be required to account for every expense incurred while volunteering for a fire department. It would appear that if a fire department intends to reimburse volunteers on the basis of reimbursement of expenses that the fire department must be able to prove that each volunteer has incurred expenses for each call, drill or other unit of service equal to or in excess of the established rate. This probably would result in a situation where a fire department could not pay its volunteers on an equal basis but would have to establish a payment schedule for each volunteer based on an itemized expense list submitted by the volunteer. While an accountable plan does not generate reportable income for a volunteer the approach is not widely used because of the challenges of accounting for all expenses. The current IRS regulations establishing the rules for accountable plans can be found in IRS publication 463.

**Nominal Sum per Unit of Service.** Instead of requiring each volunteer to account for all expenses, many fire departments establish a nominal sum per unit of voluntary service and pay such sum for each drill, response or other events at which the volunteer provides service. The determination of what constitutes a nominal sum is up to the reasonable discretion of the board of commissioners.

In 2006, the Department of Labor established safe harbor guidelines by defining what would be considered nominal payment (see below). The regulations provide that where fire fighters receive more than a nominal amount or where payment is on a basis which does not reasonably approximate the expenses incurred by them, they are considered employees rather than volunteers and therefore must be paid in accordance with the requirements of the Fair Labor Standards Act including the minimum wage and overtime provisions. If the Fire department stays within the limits of guidelines discussed below the volunteers will retain their volunteer status.

**Point or Unit System.** Many fire departments currently compensate volunteer fire fighters under a point or unit system. Under the system, each volunteer earns points or units of credit for performing various functions for the fire department. Each year the fire department budgets a specific amount for compensation to volunteer fire fighters and annually or periodically the funds are distributed on the basis of the number of points or units that each fire fighter has accrued. With certain modifications, this system is workable under the FLSA. To avoid the minimum wage problem, the following factors should be considered:

1. The fire department should award only one point or unit per activity. Do not award points or units based upon the amount of time spent by any volunteer in performing services for the fire department.
2. Points or units could be awarded for each drill attended, each alarm responded to, each meeting attended, or for the performance of any activity that the fire department may require.
3. A maximum dollar limitation per point or unit must be established.
4. The fire department could, in addition, still reimburse volunteers for actual out of pocket expenses, such as items of clothing that the fire department requires the fire fighter to provide.

### **Nominal Fee Guidelines**

In 2006, the Administrator of the Wage And Hour Division of the Employment Standards Administration issued a letter to the President of the International Association of Fire Chiefs that provides specific guidelines defining the concept of a nominal sum. A summary of the guidelines follows:

A fire department may pay its volunteers a sum not to exceed twenty percent of what it pays its paid fire fighters for similar services. If a fire department has no paid fire fighters, it may use the amount paid by nearby fire departments. Factors that may be considered in determining nominal compensation per unit of service include “distance traveled, time and effort expended, around-the-clock versus limited availability, throughout the year versus upon request”.

**Caution** – A fire department still cannot pay a volunteer an hourly wage. The payment must be based on a “unit of voluntary service” such as a drill, response, etc and should not be based on the time spent in performing the service.

The following hypotheticals were included by the Administrator as examples of acceptable nominal sum payments (provided that the total dollar amount paid was less than the 20% threshold):

- A volunteer is paid \$1,200 per year regardless of the number of shifts or amount of time spent responding to calls. On average the volunteer staffs a minimum of 24 shifts and/or spends a minimum of 60 hours responding to calls annually.
- A volunteer is paid \$100.00 per month regardless of the number of shifts or amount of time spent responding to calls. On average the volunteer staffs a minimum of 4 shifts and/or spends a minimum of 8 hours responding to calls monthly.
- A volunteer is paid \$100.00 per month so long as the volunteer staffs a minimum of 2 shifts and /or spends a minimum of 5 hours responding to calls during the month. Additional payments of \$25.00 are made for each additional shift over 4 during the month and/or for every 2.5 hours spent responding to calls exceeding 12 hours during the month.
- A volunteer is paid \$25.00 (or \$30.00 or \$40.00) for each four-hour block of time regardless of the actual amount of time below four hours spent at the station house or responding to calls.
- A volunteer is paid \$20.00 for each shift regardless of the length of the shift or the time spent responding to calls. On average, the volunteer works a 6 hour shift and/or spends 2 hours per shift responding to calls.
- A volunteer is paid \$25.00 if the volunteer staffs a shift of a least 8 hours and/or spends 2.5 hours responding to calls. An additional \$15.00 per shift is paid if the shift exceeds 8 hours or responds to calls over 5 hours during a single shift.

## **PART II - TAXATION OF VOLUNTEER COMPENSATION**

**Income Tax.** Payments made for drills and responses, regardless of whether the fire department calls it a payment of a nominal sum per unit of voluntary service or an expense reimbursement under a non-accountable plan, must be reported on form W-2 as income. Effective July 1, 1990, the Internal Revenue Service adopted regulations relating to the tax status of expense reimbursements. Basically, the regulations provide that if reimbursement of itemized expenses is paid under an "*accountable plan*" there are no tax consequences to the employee. Expense reimbursements paid under a non-accountable plan are treated as income. A fire department's reimbursement to its volunteer fire fighters is not normally paid under an "*accountable plan*" since the volunteers do not itemize the actual out-of-pocket expenses they incur in providing service to the fire department.

The regulations further provide that if the reimbursement is paid under a "*non-accountable plan*", such as that used by most fire departments, the amount is treated as income paid to the volunteer employee. As stated above, the reimbursement must be reported as taxable income on form W-2. The regulations provide that the employee (volunteer) may claim an offsetting business expense deduction provided the expenses actually incurred by the volunteer are

classified as deductible business expenses by IRS and provided that the volunteer has sufficient records to prove the expenses claimed. The restrictions and limitations on the deductibility of employee incurred expenses will apply in all situations. The fire department must require that each volunteer who receives such payments complete a form W-4 for the fire department, upon commencing volunteer status.

If firefighters are paid once a year, the annual pay period on the withholding table contained in publication 15 (circular E, Rev. January 2008) is applicable. Under that provision a single person who receives \$2,650 or less during the year would not be subject to federal income tax withholding by the Fire department and a married person who receives \$8,000 or less also would not be subject to withholding. The actual amount of reimbursement received by the firefighter, however, must be reported on a W-2 and included on the individual's federal income tax return.

Effective for 2008, 2009 and 2010, IRS Code Section 139B excludes up to \$30.00 per month of qualified payments to a volunteer from income tax. Accordingly for a volunteer serving 12 months a maximum \$360.00 of qualified payments would not be included in box 1 of the W-2 form.

**FICA.** IRC section 3121(b)(7)(F)(iii) exempts from FICA compensation paid to employees serving on a temporary basis in case of fire, storm, earthquake, flood or other similar emergency. There is a question whether this exemption covers compensation paid to volunteers for drills and responses or only for emergency responses. There is a 1992 written directive from OASI that concludes that all drills and responses are exempt. The Seattle IRS office, however, has rejected this determination and claims that regularly serving volunteers do not fall within this exemption and therefore all volunteer firefighter reimbursements are subject to FICA.

The other issue under FICA is whether volunteers meet the definition of employee under IRC 3121 The Federal, State and Local Government "FSLG" division of the IRS takes the position that volunteers are employees and therefore all volunteer payments are subject to FICA. I note that this position is an interpretation of the statutory language and, to date, there are no IRS regulations or judicial decisions directly supporting the FSLG position. If the volunteer is a member of a qualified retirement system of the fire department the Social Security tax portion would not be applicable. However, the Volunteer Fire Fighters' Pension System in Washington State is not considered a qualified retirement system.

The IRS is the only governmental agency that attempts to treat payments to volunteers in a manner similar to the payment of wages. Under the FLSA, FUTA, the State Unemployment Tax system, and under Washington court decisions, volunteers are not considered to be employees. Given the ambiguity in the IRS code provisions, it is our opinion that volunteer payments, which are based on a nonaccountable expense reimbursement concept, should remain exempt from FICA. Because of the IRS's current position, however, unless a Fire department is willing to

challenge the IRS or risk future interest and penalties if the IRS position is upheld, any decision not to pay FICA taxes on volunteer payments is not currently recommended.<sup>1</sup>

Finally, it is important to note that IRC section 139B, discussed above, which exempts up to \$360.00 of qualified payments to volunteers from income also exempts the \$360.00 from FICA. The IRS has yet to issue any regulations guiding fire departments on the proper method of reporting the excluded income.

**Federal Unemployment Tax Act (FUTA).** Compensation paid to volunteers is not covered.

**Industrial Insurance (Workers' Compensation).** Compensation paid to volunteer fire fighters is not covered unless the fire department elects coverage.

**Volunteer Firefighters Relief System.** All volunteers must be enrolled in the Volunteer firefighters relief system through the Board for volunteer firefighters.

**Volunteer Firefighters Pension Systems.** The volunteer pension system must be made available to all volunteer fire fighters who wish to participate.

**State Unemployment Tax** Although not specifically defined by statute, since payments made to volunteers are not "wages," volunteers do not meet the definition of employment and are neither eligible for unemployment benefits nor is the Fire department required to report or pay unemployment taxes for volunteers. Most fire departments elect to make payments in lieu of contributions so would not report any employee. If you have not elected to make payments in lieu of contributions, it is my opinion that volunteer payments would, nonetheless also be exempt.

The above article is a summary of a number of complex laws and regulations and is not intended as legal advice. Fire departments attempting to address these issues should consult with the department's legal counsel.

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<sup>1</sup> In March 2008, the State Auditor adopted the position of the FSLG division and now recommends that volunteer payments be subjected to social security and medicare. See Part 3, Chapter 8, Section G of the BARS manual effective 3/15/08. However, as of the date of this article the Auditor may be considering withdrawing this provision from the BARS manual.