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KPMG report: Employers providing employee hardship assistance related to coronavirus (COVID-19)

President Trump on March 13, 2020, declared the coronavirus outbreak to be a national emergency. This declaration not only frees up resources that the federal government may use to address the crisis but also expands the options that businesses have at their disposal to help employees hit by hardship as a result of the virus. Options for employers include providing assistance to employees directly or doing so indirectly through existing or newly formed public charities or private foundations.

This report reviews the options for employers, and some of the advantages and disadvantages of each.

Direct assistance from employers to employees

Relief payments

As a general rule, amounts provided by an employer to an employee are considered taxable compensation to the employee and a deductible business expense for the employer. However, when a federal “qualified disaster” has been declared, an employer may make “qualified disaster relief payments” (QDRPs) to employees, and the assistance may be excluded from employee income under section 139 (while also being deductible to the employer). QDRPs can include reimbursements of certain reasonable and necessary expenses incurred as a result of a qualified disaster. For these purposes, a “qualified disaster” includes a disaster or emergency that the president has determined warrants assistance by the federal government, as was recently declared of the coronavirus pandemic.

QDRPs do not include payments for expenses that are already being reimbursed by insurance (or otherwise) and generally do not include income replacement such as lost wages (see section 139(b)). QDRPs also, by definition, do not include payments made to assist employees with hardships that are not a result of a qualified disaster.

However, certain employer payments for additional expenses resulting directly from the coronavirus would qualify as QDRPs. For example, if essential personnel are required to report to a work location, reimbursement of additional travel expenses that are incurred due to efforts to prevent the spread of the coronavirus may potentially be excluded from the employee’s income as a QDRP. Because the

coronavirus is the first domestic communicable disease that has been declared a federal disaster, there is some ambiguity regarding exactly which payments will be considered to be “as a result of” the disaster.

Employer loans

Many employers offer loans to their employees to cover unforeseen expenses. Proceeds of a bona fide loan are generally not considered taxable income to the borrower, but the terms and circumstances of an employer-provided loan need to be carefully considered to determine whether—and when—treatment as taxable compensation may be required.

Indirect assistance through funding charitable organizations

Alternatively, an employer may fund a related or an unrelated 501(c)(3) charitable organization to provide assistance to employees. In the case of a qualified disaster in particular, funding a charitable organization to provide employee assistance would not necessarily provide additional tax benefits to the employer or the recipient employee (i.e., the payment might be deductible for the employer and excluded from income for the employee in any case as a QDRP), but it can give employees the option of also making tax-deductible contributions to a relief fund for fellow employees. And a broader range of assistance may be provided for employees—not just assistance in response to a qualified disaster—if the program is operated by a public charity.

All charitable organizations that operate an employee assistance program must satisfy the following requirements to determine that the program is operated to further their charitable purposes and not to benefit the employer inappropriately:

- **There must be a charitable class.** The class of potential beneficiaries of the program must be large or indefinite. If the group of eligible beneficiaries is too small and readily identifiable, the private benefit to those particular individuals would be too great to be permissible for a charitable organization.
- **There must be a determination of need.** The recipients must be selected based on an objective determination of need, and the organization must maintain adequate records to demonstrate the recipients’ need for the disaster assistance provided.
- **The recipients must be selected by an independent selection committee or an adequate substitute.** The charity’s selection committee is independent if a majority of the members of the committee consists of persons who are not in a position to exercise substantial influence over the affairs of the employer. And an adequate substitute would require a process to ensure that any benefit to the employer is incidental and tenuous.

If these requirements are met, the charitable organization’s payments to employees are presumed to be made for charitable purposes and not to result in taxable compensation to the employees. And a contribution made by an employer may be deductible provided the other requirements for deductibility are met.

Importantly, different rules apply depending on the type of charity providing the assistance—affecting both the type of assistance that can be provided and the tax benefits available. Although there are rules common to all section 501(c)(3) charitable organizations that provide assistance to individuals, there are also specific rules applicable to public charities, private foundations, and donor advised funds (and the sponsoring organizations that host them) that are especially likely to apply when the employer controls or is the primary donor to the organization or fund.

Employer-sponsored private foundations

Many employers already have a company foundation in place, making it a natural and easy choice to operate the employer's employee assistance program. However, if the company foundation is a "private foundation" (which will generally be the case if substantially all of its funding has come from the employer or a narrow base of donors), specific rules—backed by excise taxes on the foundation, the company (as donor), and potentially those individuals that manage the foundation—limit the assistance the foundation can provide. If a private foundation is operating an employee assistance program, the program must meet the following two additional criteria:

- **Payments may be made only to those affected by "qualified disasters."** The IRS has taken the position that employer-sponsored private foundations may not make payments to employees or their family members in emergency hardship situations that are not the result of a qualified disaster.
- **Payments may not be made to "disqualified persons."** Payments are not to be made to (or for the benefit of) individuals who are directors, officers or trustees of the private foundation or members of the private foundation's selection committee, nor can payments be made to family members of these individuals.

Employer-sponsored donor advised funds

An employer might also look to a community foundation or other public charity that sponsors donor advised funds to operate an employee assistance program. Generally speaking, a donor advised fund (DAF) is a separate fund or account that is owned and controlled by the sponsoring organization (which must be a public charity), but the donor to the fund (or an appointed advisor) has the privilege of making recommendations regarding distributions from the fund. As a general rule, a DAF may not make payments to individuals, but in Notice 2006-109, Treasury and the IRS provided an exception to this rule for employer-sponsored funds that make hardship relief payments to employees and their family members and abide by restrictions very similar to those of a private foundation, namely:

- **Payments may be made only to those affected by qualified disasters.** More specifically, the fund must serve the single identified purpose of providing relief from qualified disasters.
- **Payments may not be made to disqualified persons.** For these purposes, disqualified persons include any director, officer or trustee of the charity sponsoring the fund or any member of the fund's selection committee.

Employer-sponsored and independent public charities

A final option would be for the employer to fund an employee assistance program operated by an independent or an affiliated public charity. Public charities generally receive support from a larger number of donors than private foundations; independent public charities would have independent professionals in management and governance roles, rather than donors or their representatives. One advantage of this option is that the program would not have to be limited to assistance for qualified disasters and could make payments for a broader range of employee needs.

One obstacle to this option is ensuring that the public charity receives donations from a broad enough base of donors to qualify as a public charity. Typically, this would mean that the organization receives significant support from employees and not only the employer. (Tax incentives for contributions to public charities are generally more generous for individuals and businesses than the incentives for contributions to private foundations.) Some companies have established affiliated public charities to facilitate employee charitable giving and employee-to-employee assistance, in addition to company assistance. Some independent public charities operate several employee assistance programs, funded

by different employers. Note, however, that if an employer has excessive input on the distribution of funds, and the employer, rather than the charity, is considered to be making the determinations regarding recipient needs, the program could be considered to be a DAF, exposing the donor and the sponsoring organization to potential excise taxes if it does not operate in accordance with the DAF restrictions. Therefore, care must be taken to determine an employee assistance program at an independent public charity does not allow excessive donor advisory privileges.

Assistance from employees

Facilitating employee-to-employee gifts

Employers may facilitate employee-to-employee giving, by pooling these payments (generally in a separate bank account), and making the employee gift payment separate from any employer assistance payment. Because the employer is acting as the agent of the donor-employees in aggregating the contributions, the recipient-employees may presumably exclude these gifts from income. However, the donor-employees make their contributions with after-tax dollars and may not take charitable contribution deductions for amounts given to individuals. Because of these potential negative tax consequences, as noted above, an employer may set up an affiliated public charity to facilitate employee-to-employee assistance.

Leave-sharing plans

Employers can also set up leave-sharing plans that allow employees to surrender accrued hours of paid leave for the benefit of other employees dealing with "medical emergencies" or dealing with hardship caused by a federally declared "major disaster." (As of this writing, the coronavirus was being declared a "major disaster" on a state-by-state basis, as states such as New York, California, and Washington requested and obtained such a declaration. For a listing of states that have been declared a major disaster, see the [FEMA webpage](#).) Under long-standing IRS guidance, employees who donate leave to other employees for such hardships through an employer leave-sharing plan may exclude the value of the leave from income, provided the recipient-employee includes such value in income. In the absence of a federally declared major disaster, employers may still set up a leave-sharing program to benefit employees suffering "medical emergencies."

Leave-based charitable donation programs

Finally, the IRS has occasionally issued guidance allowing employees to forgo leave and exclude the cash value of the leave from income if their employers agree to contribute the cash value of the leave to a charitable organization that benefits the victims of a specified disaster. (The employees cannot, however, take a charitable contribution deduction for this donated leave.) No such guidance has yet been issued with respect to the coronavirus.

KPMG observation

Because the coronavirus has been declared a disaster by the federal government, employers have an expanded range of options for structuring assistance for employees suffering hardships as a result of the virus.

For more information, contact a KPMG tax professional:

Exempt organizations:

Ruth Madrigal | +1 202 533-8817 | ruthmadrigal@kpmg.com
Preston Quesenberry | +1 202 533-3985 | pquesenberry@kpmg.com

Development and exempt organizations:

Shannon Kirkpatrick | +1 225 379 5017 | skirkpatrick@kpmg.com
Anita Whitehead | +1 703 286 8245 | awhitehead@kpmg.com
Lori McLaughlin | +1 864 250 2620 | lamclaughlin@kpmg.com
Chad Franks | +1 213 955 1521 | chadfranks@kpmg.com

Compensation and benefits:

Robert Delgado | +1 858 750-7133 | rdelgado@kpmg.com
Erinn Madden | +1 202 533-3757 | erinmadden@kpmg.com
Terri Stecher | +1 202 533-4830 | tstecher@kpmg.com

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