The following is for use by assistive readers and users who prefer a text version of this course.

Providing Disaster Relief Through Charitable Organizations – Part II

Page 1 – Welcome

The following is a fictitious discussion between Coach, the knowledgeable, straight-talking IRS Revenue Agent from the website, StayExempt.org, and representatives of tax exempt organizations at a community meeting to discuss Disaster Relief efforts.

Page 2 – Course Objectives

This is Part II of a two-part mini-course on Providing Relief Through Charitable Organizations. Part I discusses how charitable organizations may provide disaster relief and the tax law that generally applies to such tax-exempt organizations. You should review the materials in Providing Disaster Relief Though Charitable Organizations, Part I, before you start Part II.

This section of the mini-course will address the special rules that apply to the provision of assistance by employer sponsored charitable organizations, the law governing the deductibility of contributions for disaster relief purposes, and the income tax treatment of payments to disaster victims.

This program is brought to you by IRS Exempt Organizations.

Page 3 – Welcome

Bert: Hey, Coach, welcome back to our Nonprofit Tax Law Clinic.

Coach: Thanks for having me. I'm glad to be back to talk to you about some of the more complex issues involved in providing assistance to disaster victims about getting help to the victims. Last time we discussed the basics of providing assistance through charitable organizations but I know some of you small business owners had questions about providing assistance to your employees.

Dakota: That right, Coach. I'm a small business owner and I want to be able to help my employees in times of need. How can we be prepared to help our employees if a disaster strikes or if an employee suffers a personal tragedy like losing a home in a fire or a sudden death or serious illness in the family? Should we set up our own charity or just make direct payments to those in need?

Coach: Good question. You can help in a number of ways. The type of assistance you intend to provide will help you determine the best vehicle for giving.

Bert: What do we need to consider?

Page 4 – Employer-Sponsored Charities

Coach: You'll need to consider the following:

- whether you intend to provide help in both disaster and personal emergency situations
- whether you intend to seek contributions from employees and the general public or your company will be the primary or sole contributor
- whether it is preferable to provide direct assistance without setting up a charitable organization

Bert: What kind of vehicles can we use to give and how do they differ?

Page 5 – Employer-Related Charities

Coach: You can:

- establish an employer-sponsored public charity
- set up an employer-sponsored private foundation
- create a donor advised fund
- make payments directly to the employees

Each of these options is subject to certain restrictions, so let's talk about them one at a time.

Page 6 – Employer-Sponsored Charities

Before we do, keep in mind that, if you intend to provide assistance through a tax-exempt organization, it's important to show that the employer does not control the selection of aid recipients.

Like all 501(c)(3) organizations, disaster relief organizations cannot confer a private benefit on any individual. If the employer controls the selection of recipients, the charity could be viewed as a means of helping the employer recruit and retain employees, resulting in an impermissible private benefit to the employer. That's why it is important to ensure that you, as the employer sponsor, do not control the selection process, regardless of what type of charity you intend to create or use.

Another area of concern is whether a payment from the employer or the employer-sponsored charity to the employee is taxable compensation from the related employer or it is considered a gift or is otherwise excluded from the recipient's income.

Page 7 – Employer-Sponsored Public Charities

Dakota: Okay, begin with the employer-sponsored public charity.

Coach: Employer-sponsored public charities have the most flexibility of the four options I mentioned. Like any public charity, which solicits contribution from various sources, an employer-sponsored public charity can provide broad assistance in disaster situations – like a hurricane or other natural disaster or civil disturbance – or in an emergency or personal hardship situation, such as when an employee suffers from a sudden death or serious illness in the family.

Bert: How do we have to set up our employer-sponsored public charity to ensure that it will qualify for exemption and it doesn't appear that it is operating for the benefit of our company when we make payments to employees?

Page 8 – Employer-Related Public Charity

Coach: An employer-sponsored public charity will be presumed to be operating for charitable purposes and not for the private benefit of the employer if it can show that:

- it serves a charitable class
- the recipients are selected based on an objective determination of need or distress
- the recipients are selected by an independent selection committee or by some similar procedures designed to ensure that any benefit to the employer is incidental

Bert: How do we show that the selection committee is independent?

Page 9 – Employer-Related Public Charity

Coach: If the majority of the committee consists of persons who aren't in a position to exercise substantial influence over the affairs of the employer, the charity's selection committee will be considered independent.

As you'll remember one of the big issues that is raised in the operation of an employer-sponsored charity is whether payments to employees are considered to be part of an employee's compensation and taxable as income. It's important to demonstrate that your recipient selection process is independent of the employer-sponsor to show that the benefits provided under the relief program aren't just part of the employee's compensation package.

Dakota: So, if we meet all of the requirements we just discussed, the payments will not be considered to be compensation and treated as income to the employee recipients?

Coach: That's right!

Page 10 – Employer-Sponsored Private Foundations

Dakota: How do the rules differ if we don't intend to solicit contributions from other sources?

Coach: Then your organization would probably be an employer-sponsored private foundation. Several issues arise when a private foundation provides aid to employees when the employer is a substantial contributor to the private foundation. We have to think more about potential private benefit and potential liability for the foundation excise taxes on self-dealing. In addition, we must consider whether the payment is compensation to the employee, a gift, or other type of payment that is excluded from income.

Bert: Are there any restrictions on the type of assistance we can provide through an employer-sponsored private foundation?

Coach: Unlike employer-sponsored public charities that can provide relief to employees and their families in any emergency hardship or disaster situation, employer-sponsored private foundations can only provide support in response to a "qualified disaster." They cannot make payments to individuals in emergency situations like a house fire or severe illness of an employee's child.

Bert: Please clarify what is considered a "qualified disaster," since employer-sponsored private foundations can only provide support in these instances.

Page 11 – Qualified Disaster

Coach: A qualified disaster is a disaster that:

- results from terrorist or military actions
- results from an accident involving a common carrier
- is a presidentially declared disaster
- is deemed catastrophic by the Secretary of Treasury

Page 12 – Employer-Sponsored Private Foundations

Dakota: How can we make sure that we're not viewed as engaging in self-dealing if our employer-sponsored private foundation makes payments to employees and their families?

Coach: If the employer is a substantial contributor to the private foundation, the IRS will presume that the private foundation's payments to employees are made for charitable purposes if:

- the potential beneficiaries are chosen from a charitable class
- the recipients are selected after an objective determination of need or distress
- the selection is made by an independent selection committee or similar procedure

If these requirements are met, then the payments won't result in prohibited self-dealing merely because a recipient is an employee – or family member of an employee – of an employer-sponsor. Plus, the payments won't be considered to be compensation taxable to the employee.

Bert: What if we make a payment to a family member of one of the members of the selection committee?

Coach: A payment to a member of the selection committee or an officer or director or one of their family members wouldn't come under the limited exception to the self-dealing rules and would be subject to tax under the self-dealing rules.

Page 13 – Donor-Advised Funds (DAFs)

Dakota: Earlier, you mentioned donor advised funds as another way employers can help their employees. What are donor advised funds and how can they help?

Coach: Certain community foundations and public charities maintain separate funds or accounts to receive contributions from individual donors who can exercise limited rights to advise as to how their donated funds are to be invested or distributed. Also, they normally cannot make grants to individuals either. That is why they are called donor-advised funds.

Page 14 – Employer-Sponsored Donor-Advised Funds (DAFs)

While these funds generally can't make grants to individuals, employer-sponsored donor advised funds can make grants to individual employees and their family members if the fund:

- serves the sole purpose of providing relief from one or more "qualified disasters"
- serves a charitable class
- selects recipients based on an objective determination of need
- selects recipients using an independent selection committee or equivalent procedure designed to ensure that any benefit to the employer is incidental or tenuous
- maintains adequate records to show the recipients need for the disaster relief

Page 15 – Question

Dakota: How can our business help our employees if we don't want to go through an existing qualified charitable organization or start a new organization but want to make sure that the individual recipients aren't taxed on the assistance we provide?

Page 16 – Direct Giving by Employers and Others

Coach: Anyone, including an employer, can make "qualified disaster relief payments" to cover reasonable and necessary personal, family, living or funeral expenses incurred as a result of a disaster. In addition, one can make payments for reasonable and necessary expenses incurred for the repair of a personal residence and for the repair or replacement of the contents of a personal residence in a declared disaster.

Page 17 – Taxability of Assistance

Dakota: If I receive disaster relief assistance from a charity, is that considered income and subject to tax? What about aid I receive from a charity related to my employer?

Coach: Payments you receive from a qualified charity are considered gifts and are not included in your gross income. Also, as long as a charity related to your employer follows the selection guidelines we discussed earlier, the payments you receive won't be considered to be compensation to you or be taxable as income.

Bert: What if my business received help? Is that considered a gift?

Coach: The IRS will generally consider the facts and circumstance surrounding a charity's payment to a for-profit business. We'll consider whether the charity intended the payment to be a gift or whether it was made in anticipation of services to be provided later or as some other legal or moral obligation. It all comes down to intent. If it wasn't intended to be a gift, it will be considered income.

Page 18 – Question

Dakota: I want to make a contribution to a local disaster relief organization. Will my contribution be deductible?

Coach: If you make a contribution to a qualified domestic charitable organization and you file an itemized tax return, you may be eligible to claim a federal income tax deduction for the contribution.

Page 19 – Contributions

Bert: How do I find out if the organization is qualified?

Coach: Go to the *Charities and Nonprofits* pages of IRS.gov and click on the search for charities link. There, you'll find an electronic list of qualified organizations entitled to receive tax deductible contributions. Or if you prefer, call (800) 829-1040, toll free.

Dakota: Do I need any receipts or anything to claim a charitable deduction?

Coach: You need a record, such as a bank record like a cancelled check, or a receipt or letter from the charity, acknowledging the contribution in order to claim a tax deduction. For more information about contributions you can download Pub. 526, *Charitable Contributions* at IRS.gov.

Also, if your contribution is $250 or more, you must have a contemporaneous acknowledgement from the recipient organization in order to claim a tax deduction.

Bert: What kind of acknowledgment does our organization have to give our donors?

Coach: No particular language is required. Check out Publication 1771, *Charitable Contributions, Substantiation and Disclosure Requirements* for additional information about the substantiation and disclosure requirements.

Page 20 – Foreign Activities

Dakota: Can I take a tax-deduction for a contribution I make to a foreign organization or a US charity that does disaster relief work overseas?

Coach: Contributions to foreign organizations are generally not tax deductible unless permitted under a tax treaty. Currently, the US has tax treaties with Canada, Mexico and Israel.

You can take a tax deduction for a charitable contribution made to a US charitable organization that does work abroad, as long as the US organization maintains full control and discretion over the use of the funds.

Page 21 – Gifts to Individuals

Bert: A guy in our office had a car accident and can't afford a down payment for a new car. If I make a contribution to his 'new car fund' is my contribution tax-deductible?

Coach: No. Any monies you contribute to the new car fund would simply be considered a gift to your co-worker, not a charitable contribution. But sometimes that's the best way to accomplish your goal in a situation like this.

You can't deduct any monies you give to your co-worker's new car fund as a charitable contribution on your federal income taxes. Remember, the new car fund isn't a qualified charitable organization entitled to receive charitable contributions and your co-worker wasn't selected from among the members of a charitable class. Also, a payment that is deductible as a charitable contribution cannot be earmarked for a particular individual like your co-worker.

Page 22 – Conclusion

Dakota: Thanks, Coach. You've given us a lot of good information. Where can we find additional information?

Coach: Thanks for giving me the opportunity. If you want to review some of the material we've discussed today go to our website www.irs.gov/charities and download a copy of Publication 3833, *Disaster Relief: Providing Assistance Through Charitable Organizations* and some of the other publications and mini-courses we've mentioned today. You can learn more about charitable contributions by viewing our StayExempt Mini-Course, *Can I Deduct My Charitable Contribution?*

Take care now, and call our toll-free number at 877-829-5500 if you have any further questions.

Page 23 – Resources

Go to www.irs.gov/charities for the following publications:

- Publication 3833, *Disaster Relief*
- Publication 557, *Tax Exempt Status for Your Organization*
- Publication 526, *Charitable Contributions*
- Publication 1771, *Charitable Contributions: Substantiation and Disclosure*
- Publication 4221-PC, *Compliance Guide for 501(c)(e) Public Charities*
- Publication 4221-PF, *Compliance Guide for 501(c)(3) Private Foundation*
- www.StayExempt.org for other mini-courses on special topics
- www.irs.gov/eo for Form 990 and Schedules