

CORONAVIRUS

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Key Considerations for Creating Employer-Sponsored Charities in Response to the COVID-19 Crisis

With the growing impact of COVID-19, industries across America are laying off numerous workers, who will be without jobs and income for an undetermined period of time. As this crisis plays out, many business owners are interested in providing financial assistance to their furloughed or terminated employees even though they cannot afford to keep them on payroll. An attractive option is the creation of an “Employer-Sponsored Charity” to raise tax-deductible contributions to be distributed to former employees with demonstrated need. As part of evaluating whether this type of charity is appropriate for your company, below are some of the key considerations and steps needed to successfully create such an entity and obtain the critical IRS classification as a 501(c)(3) tax-exempt organization:

Charitable Class: The IRS will not authorize charities that support identifiable individuals for a single purpose. However, charities benefitting individuals are permissible if the class of eligible beneficiaries is broad enough to be considered “indeterminable.” For example, a charity designed to benefit the displaced employees of a single restaurant due to COVID-19 is not a broad enough charitable class because the beneficiaries can be easily identified. However, a charity designed to benefit past, current, and future employees of an entire restaurant group due to COVID-19 and future disasters is broad enough. Here, the beneficiaries

are not immediately identifiable because unknown future employees and current employees who are victims of future disasters are eligible beneficiaries.

Awarding Grants: Although the charity is designed to provide funds and other assistance directly to employees, it is important that a number of steps are followed. First, the individuals vested with the authority to make grants—either the board of directors or a committee appointed by the board of directors—must consist of a majority of individuals who do not exert “substantial influence” over the business with rank-and-file employees included among the decision makers. We also recommend that the number of individuals on the board or committee be an odd number, *i.e.*, five or seven, to avoid the possibility of tie votes. Most importantly, the criteria for awarding grants should be written, objective, and followed without exception.

Use of Grant: Individuals who demonstrate financial need are eligible to receive assistance, but a charity should avoid giving a one-size-fits-all grant to every employee. Terminated employees with independent wealth should not be eligible. Acceptable purposes for grants include payment of necessary healthcare expenses; providing costs of childcare or educational expenses for children of employees; or short-term grants meant to cover basic living expenses.

The charity should retain documentation regarding the employee's eligibility for a grant and verification that the employee used the funds for eligible purposes. Charities can also provide direct services such as crisis counseling and meals.

Process: Creating an organization recognized as a 501(c)(3) tax-exempt organization requires following a number of steps under state and federal law. The first step is creating a not-for-profit corporation. The corporation should be created either in your home state or in a state like Delaware, with its flexible corporate law and easy incorporation process. **After this step is complete, the IRS treats all donations to the charity as tax deductible provided you timely submit your IRS application and it is approved.** (If you incorporate out of state, as many charities do, you will eventually need to qualify to do business in your home state, but this can be done without delaying the remaining steps.) The next step is to open a bank account in the name of the charity and complete all organizing documents (*i.e.*, Bylaws, Resolutions Appointing Directors and Officers, Conflict-of-Interest Policy, Grant-Making Policy, etc.), which need to be submitted with your IRS application. The application to the IRS—known as Form 1023—can then be filed. Although the IRS review process generally takes up to six months, charities that provide disaster relief are eligible to obtain approval on an expedited basis. We believe employer-sponsored charities created to help those financially impacted by COVID-19 should qualify for expedited review, which is important because although donations are treated as tax deductible beginning with the day of incorporation, larger donors—especially other charities—may be reluctant to provide support until the IRS issues a determination letter awarding 501(c)(3) status. There are also a number of state-law requirements, most importantly, the requirement in many states to register prior to soliciting contributions. Finally, applicants with projected gross receipts of \$50,000 or less for each of the first three years of operations are eligible to file a streamlined version of the exemption application (Form 1023-EZ).

Subclassification: Not all charities are created equal. Section 501(c)(3) tax-exempt organizations are subclassified as either private foundation or public charities. Generally, private foundations receive support from either a handful of individuals or a single family and are therefore subject to additional IRS restrictions. (As an alternate, employers may be able to assist their employees by making qualified disaster relief payments on a tax-free basis under Section 139 of the Code.) Public charities receive a broad base of support from the general public—including other charities, the government, and individuals—and are therefore not subject to the restrictions imposed on private foundations. Additionally, an employer-sponsored public charity could be created to assist its employees through the COVID-19 crisis and future emergency hardship situations regardless of whether a future hardship is caused by a federally designated qualified disaster.

Employer-sponsored charities are an attractive option that business owners can use to help individuals that have been loyal to them and contributed to the success of their company. The [Tax, Benefits, and Private Client](#) group of Blank Rome LLP is ready to counsel and help clients navigate these rules and create charities designed for success.

Blank Rome's Coronavirus ("COVID-19") Task Force is continuing to monitor the COVID-19 crisis and will provide further updates for business owners as they become available.

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