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Employee Financial Assistance During the COVID-19 Crisis

The current COVID-19 pandemic has been devastating on many levels, including for employees across industries. Many of our clients are thinking about how they can support their teams during this unprecedented crisis and have inquired about employee financial assistance programs. Organizations ranging from restaurants to private equity firms are establishing employee relief funds as a way to provide direct financial support — and, often, for other individuals to contribute — to their employees. Family offices and sponsors are also encouraging and supporting their investments and portfolio companies to do the same.

Often referred to as Employee Assistance Funds, Employee Relief Funds or Employee Crisis Funds, these programs that family offices, employers and sponsors establish provide financial assistance to individuals in times of disaster. As one example, on March 19, 2020, Leonard Green & Partners pledged \$10 million to a program for employees impacted by COVID-19.

There are various ways to form these assistance programs and, depending on the structure, they can provide tax efficiencies for the donors and/or the fund recipients. Below are several example structures, including benefits and potential drawbacks of each, to consider when evaluating the creation of an employee assistance program.

Option 1: Qualified Disaster Relief Payments from Employers

A family office that directly employs personnel may consider making “qualified disaster relief payments” to its employees pursuant to Section 139 of the Internal Revenue Code. To the extent that relief payments are expected to come from the employer rather than from donations from other employees, this is the most expedient and efficient method to provide relief to affected employees.

Qualified disaster relief payments by an employer are deductible to the employer and are excluded from the income of the recipient (and, therefore, any such payments are not subject to employment taxes or withholding).

- “Qualified disaster relief payments” are payments for, among other things, “reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster,” but such amounts cannot cover lost wages or lost business income or expenses otherwise paid for by insurance.
- A “qualified disaster” is any federally declared disaster; COVID-19, which was declared a national emergency by the president under the Stafford Act on March 13, 2020, is included in this designation.¹
- Because of the extraordinary circumstances surrounding a qualified disaster, individuals should not be required to account for actual expenses in order to qualify for the exclusion, provided that the amount of the payments can be reasonably expected to be commensurate with the expenses incurred.

Benefits

- Tax-free to the employee; tax-deductible to the employer
- Can be established and paid quickly, often within days
- Funds can be used for a wide range of matters, offsetting expenses resulting from COVID-19 (e.g., expenses resulting from working from home, additional child care or supplies)

Potential Drawbacks

- Payments (donations) must come from the employer, which may limit a family office's ability to utilize this option for related entities
- Donations from individuals or other organizations are not tax-deductible to such donors; however, they remain tax-free to the employee

Option 2: Create a New, or Utilize an Existing, Tax-Exempt Charity Organization

A family office may establish a new tax-exempt entity to qualify under Section 501(c)(3) of the Internal Revenue Code that will receive tax-deductible contributions from family members, employees or the general public for distribution to affected employees. The new entity will either be a public charity or private foundation, depending on its primary source of funding. This is an important distinction because (a) the deductibility of donations to private foundations is subject to more limitations than public charities and (b) private foundations are subject to certain excise taxes. It can often take six months or longer to receive confirmation of tax-exempt status from the IRS; however, the organization can solicit donations and distribute grants while the application is pending. Any such donations will be retroactively deductible once tax-exempt status is approved.

Alternatively, a family office that has an existing foundation or other tax-exempt organization may be able to use it for the purpose of collecting funds and providing relief payments. If the organization's charter includes "general" charitable purposes, it may not need any changes to its governing documents. It is important to review the current governing documents and structure to confirm it is compliant for these purposes. An existing entity also likely has infrastructure and resources in place it can leverage to administer an additional program. This can make it much easier and faster to implement as compared to forming a new entity.

Whether new or existing, the charity organization can make grants to individual employees if the following criteria are met:

- Class of beneficiaries must be large or indefinite; practically, this means that funds cannot be limited to only COVID-19-related grants but must also potentially help employees affected by future disasters
- Recipients must be selected based on objective determination of need (simply being affected by disaster is not sufficient)
- Recipients must be selected by an independent selection committee (i.e., majority of committee members do not exercise substantial influence over affairs of employer), or adequate substitute procedures must be established
- If the foundation benefits employees of a specific company, less than a majority of the grant committee should be people who are in a position to exercise substantial influence over the affairs of the employer
- Must maintain adequate records to demonstrate payments further the organization's charitable purpose
- Additional or more restrictive requirements apply to private foundations

Benefits

- Wide base of donors beyond the family office
- An individual's donations to the organization may be tax-deductible (retroactively for a new organization and immediately for an existing organization)
- Receipt of funds by employee will be tax-free; may permit broader scope of grants than under Section 139
- Family office retains control over entire process; utilizing existing infrastructure and resources can minimize administrative expense

Potential Drawbacks

- Distribution of funds is more controlled, subject to a selection process
- Organization must be ongoing and comply with future administrative requirements (e.g., annual reporting on Form 990)
- Confirmation of tax-exempt status may take 6+ months for a new entity
- Can add complexity to existing tax-exempt entity administration (e.g., grantmaking, compliance with administrative requirements)

Option 3: Employer-Sponsored Donor Advised Funds

Certain public charities have established separate funds or accounts to receive tax-deductible contributions from donors that allow the donor to retain advisory privileges over the investment or distribution of the donated funds. These programs are similar to family office-formed tax-exempt entities (Option 2 above), but instead utilize the tax-exempt status of a third-party public charity (the “Sponsor Charity”).

Having the Sponsor Charity manage the funds removes administrative complexity and burden from the family office (e.g., Sponsor Charity acts as the independent committee that approves/rejects grant applications based upon objective criteria set up by the family office, maintains any necessary supporting information and files any required tax returns). In turn, the Sponsor Charity charges fees for establishing and managing these donor advised funds (e.g., an initial setup fee, a monthly charge, a percentage of all donations and a per grant request fee).

Benefits

- Wide base of donors beyond the family office
- An individual’s donations will be tax-deductible; receipt of funds are tax-free to recipient
- Speed of implementation; can be established in as little as 48 hours

Potential Drawbacks

- Costs and expenses could result in less funds being received by the employees
- Subject to the same selection and payment requirements as a family office-formed tax-exempt charity organization
- Family office will be required to maintain the fund for a minimum duration depending on provider contract requirements
- A limited number of donor-advised funds will make grants to individuals

While Kirkland does not maintain any relationship with or endorse any specific Sponsor Charities, some examples include:

- [U.S. Chamber of Commerce Foundation](#)
- [Emergency Assistance Foundation](#)
- [Employer Relief Fund](#)

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The above options for financial assistance programs are examples of different ways you may consider providing relief payments to employees. You should work closely with your advisors in exploring and establishing the right solution for your organization.

1. While there is some debate over the legal technicalities of applying Section 139 in the event of an emergency declaration, Section 139 relief is expected to apply. Notably, Revenue Ruling 2003-29 and other IRS guidance state that a “Federally declared disaster” includes an event declared a major disaster or an emergency under the Stafford Act.

We are thinking about you during this hard time and are here to help. Our team is compiling resources in real-time (e.g., state and local guidance for business restrictions, IRS guidance on the Families First Coronavirus Act and unemployment insurance benefits), so please reach out if we can provide anything or if you have questions. We wish you all safety and good health.

If you have questions about the topics addressed in this *Private Investment & Family Office Insights*, please contact familyoffice@kirkland.com or one of the attorneys listed below.

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