KPMG Report:

Employers providing employee assistance for victims of Los Angeles wildfires

January 2025

On January 8, 2025, President Biden approved a major disaster declaration for areas affected by wildfires and straight-line winds from January 7 and continuing in Los Angeles County, California. This declaration not only frees up resources that the federal government may use to address the disaster but also expands the options that businesses have at their disposal to help employees hit by hardship as a result of the fires. 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

Qualified disaster 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. In this respect, section 139 permits non-taxable payments for reasonable and necessary personal, family, living or funeral expenses as well as for the repair or rehabilitation of a personal residence or repair or replacement of its contents to the extent that the need for such repair, rehabilitation, or replacement is attributable to 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 Los Angeles County wildfires.

QDRPs, as defined in section 139, 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. 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 wildfires would qualify as QDRPs. For example, provision of temporary housing, meals, and basic necessities resulting from an employee's rapid evacuation from home and long-term recovery would generally qualify as QDRPs. What is reasonable and necessary may take many forms and may include:

- Temporary housing related expenses (housing itself, search fees, etc.)
- Repair or rehabilitation of housing, including cleaning supplies
- Replacing home contents as well as home office supplies,
- Additional expenses for meals, transportation, or child care and /or caregiver expenses,
- Medical expenses related to the fires not covered by insurance (for example, copays, deductibles, over-the-counter medicines),
- Expenses to enhance mental health and physical well-being that are related to the fires

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. Tax-exempt employers may be limited in their ability to provide loans to employees by federal tax and/or state charity laws.

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 foundational requirements to demonstrate that the program is operated to further their charitable purposes and not to benefit an 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. Often, to meet this requirement, charities will establish programs that will assist individual victims of current and future disasters.
- There must be a determination of need. 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 to the charitable organization made by an employer may be deductible provided the other requirements for deductibility are met.

In addition, further requirements will apply to the charitable organization's distribution of funds. These requirements differ 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 (and proposed regulations issued in 2024), Treasury and the IRS provided an exception 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, including:

- 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 certain "disqualified persons."

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 need to limit its assistance to 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 numerous companies or from employees as well as the employer. (Some companies have established affiliated public charities to facilitate employee charitable giving and employee-to-employee assistance, in addition to company assistance). Another challenge is that care must be taken to ensure that the charity, not the employer/donor, is making determinations regarding who to assist (and how) and is not merely receiving and distributing earmarked donations. If the employer/donor earmarks or retains too much control over the distribution of donated funds, the gift could be recharacterized as a payment directly to the affected employee, and if it did not qualify as a QDRP, it could be taxable as additional compensation.

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 ensure that an employee assistance program established 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. If this potential negative tax consequence is significant, an employer may set up an affiliated public charity to facilitate individual giving for employee assistance, as noted above.

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." 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.

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 Los Angeles wildfires.

Key Takeaway

Because the Los Angeles wildfires have been declared a disaster by the federal government, employers have a wide range of options for structuring assistance to employees. KPMG's Compensation and Benefits and Exempt Organizations professionals collaborate to help employers identify and implement programs to rapidly meet the needs of employees and communities in need.

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