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COUNCIL *on* FOUNDATIONS

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# **Can Corporate Giving Benefit Company Employees? Let's Find Out**

October 24, 2018

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# Presenters



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# Agenda

1. Grants to Individuals: An Overview
  2. Employer-Related Scholarships
  3. Employee Assistance/Hardship Funds
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## Grants to Individuals: An Overview

### IRC § 4945 – Taxes on Taxable Expenditures

- (d) - “Taxable expenditure” means any amount paid or incurred by a private foundation—
  - (3) as a grant to an individual for travel, study, or other similar purposes by such individual unless such grant satisfies the requirements of subsection (g)

### Penalties

- On the foundation – 20% (100% if not corrected within taxable period)
- On the management\* – 5% (50% if not corrected within taxable period)
  - \*Unless agreement by management is not willful and is due to reasonable cause.



## Grants to Individuals: An Overview

IRC § 4945(g) **Individual Grants** – Subsection (d)(3) shall not apply to an individual grant awarded on an objective and nondiscriminatory basis pursuant to a procedure approved in advance by the Secretary, if it is demonstrated to the satisfaction of the Secretary that—

- (1) the grant constitutes a scholarship or fellowship grant which would be subject to the provisions of section 117(a)...and is used to study at an educational organization described in section 170(b)(1)(A)(ii),
- (2) the grant constitutes a prize or award which is subject to the provisions of section 74(b) (without regard to paragraph (3) thereof), if the recipient of such prize or award is selected from the general public, or
- (3) the purpose of the grant is to achieve a specific objective, produce a report or other similar product, or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar capacity, skill, or talent of the grantee.





# Grants to Individuals: An Overview

## Objective and Nondiscriminatory Basis

- Must be selected from a group large enough to constitute a charitable class
- Selection should be related to the purposes of the grant
  - In the case of a scholarship, this could include academic performance, standardized test scores, recommendations, financial need, etc.
- Persons selecting grantee should not be in a position to derive a private benefit from the selection



# Grants to Individuals: An Overview

## Requirements for Advance Approval

- Grant procedure includes an objective and nondiscriminatory selection process
- Procedure is reasonably calculated to result in performance of the activities grants are intended to finance
- Foundation plans to obtain reports to determine whether grantees have performed the activities grants are intended to finance
  - If paid directly to educational institution that agrees to supervise the use of the grant, foundation is not required to obtain yearly reports from grantee



## Grants to Individuals: An Overview

IRC § 4945(g) **Individual Grants** – Subsection (d)(3) shall not apply to an individual grant awarded on an objective and nondiscriminatory basis pursuant to a procedure approved in advance by the Secretary, if it is demonstrated to the satisfaction of the Secretary that—

- (1) the grant constitutes a scholarship or fellowship grant which would be subject to the provisions of section **117(a)**...and is used to study at an educational organization described in section 170(b)(1)(A)(ii),
- (2) the grant constitutes a prize or award which is subject to the provisions of section 74(b) (without regard to paragraph (3) thereof), if the recipient of such prize or award is selected from the general public, or
- (3) the purpose of the grant is to achieve a specific objective, produce a report or other similar product, or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar capacity, skill, or talent of the grantee.



# Grants to Individuals: An Overview

## IRC § 117(a) – General Rule

- Gross income does not include any amount received as a qualified scholarship by an individual who is a candidate for a degree at an educational organization described in section 170(b)(1)(A)(ii).

## What is a “qualified scholarship?”

- Must be established that the grant was used for qualified tuition and related expenses
- Related expenses can include fees, books, supplies, and equipment required for courses of instruction
- “Fees” may also include contributed services and accommodations per Treas. Reg. 1.117-1(a).



## Employer-Related Scholarships

How Can an Employer Provide Scholarships to Employees or Children of Employees?

- Directly from the employer to employee
  - May be deductible as a business expense but is not a charitable contribution and would be treated as compensation to the employee
- Through employer's own private foundation
  - Subject to Rev. Proc. 76-47
- Through an employer-sponsored scholarship fund at a public charity, such as a community foundation
  - COF Legal strongly recommends that the strictures of Rev. Proc. 76-47 be applied



# Employer-Related Scholarships

## **Rev. Proc. 76-47**

- Establishes rules to determine whether grants made by an employer-related scholarship or fellowship program constitute scholarships or fellowship grants under IRC 117
- Applies to private foundations (although it is recommended that employer-related scholarship funds at community foundations follow apply the same test)
- Presumes that other requirements (e.g., objective and nondiscriminatory basis, charitable class) have been met – guidelines only directed to question of whether grants qualify under IRC 117.



# Employer-Related Scholarships

## **Rev. Proc. 76-47**

The IRS will treat grants from an employer-related scholarship program as scholarships or fellowship grants subject to IRC 117(a) if:

1. The availability of the grants falls outside the pattern of employment;
2. Grants do not otherwise represent compensation for past, present, or future services rendered or to be rendered by employees or their children; and
3. Grants are not for studies or research undertaken primarily for the benefit of the foundation or the employer or other purposes not sanctioned by IRC 117.



# Employer-Related Scholarships

## **Rev. Proc. 76-47 – Guidelines**

If all 7 conditions plus the percentage test are satisfied, IRS will assume that grants awarded under the program will be scholarships or fellowships subject to 117(a).

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## Employer-Related Scholarships

**1. Inducement:** Programs must not be used by the employer, the private foundation, or the organizer thereof, to recruit employees or to induce employees to continue their employment or otherwise follow a course of action sought by the employer.

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## Employer-Related Scholarships

**2. Selection Committee:** Selection must be made by a committee consisting wholly of individuals totally independent and separate from the private foundation, its organizer, and the employer concerned.

- Former employees are not considered totally independent
- Committee should consist of individuals knowledgeable in the education field
- Grants must be awarded solely in the order recommended by the committee
- May decrease but not increase number of grants recommended by committee



## Employer-Related Scholarships

**3. Eligibility Requirements:** The program must impose identifiable minimum requirements for grant eligibility.

- Requirements must be related to the purpose of the program
- For scholarships, must be limited to employees/children of employees who meet the minimum standards for admission to an educational institution for which grants are available
- Minimum employment period may not exceed three years
- Eligibility must not be related to any other employment-related factors.



## Employer-Related Scholarships

**4. Objective Basis of Selection:** Selection of grant recipients must be based solely upon substantial objective standards that are completely unrelated to the employment of the recipients or their parents and to the employer's line of business.

- E.g., Prior academic performance, standardized aptitude test performance, recommendations from instructors or other individuals not related to potential awardees, financial need, personal interviews



## Employer-Related Scholarships

**5. Employment:** Grant may not be terminated because the recipient or the recipient's parent terminates employment with the employer subsequent to the awarding of the grant, regardless of the reason for termination of employment.

- If grant is awarded for one year and recipient must reapply for subsequent years, the recipient may not be considered ineligible for a further grant because of change in employment status with employer.
- If grant is awarded for multiple years, subject to renewal, the standards for renewal must be based solely upon nonemployment related factors and may not be denied because the recipient or parent has previously terminated employment with the employer.
- Must be no requirement, condition, or suggestion at the time the grant is awarded or renewed that the recipient or parent is expected to render or be available for future employment by the foundation or employer.



## Employer-Related Scholarships

**6. Course of Study:** The courses of study for which grants are available must not be limited to those that would be of particular benefit to the employer or to the foundation.

- If available courses of study include one or more that would be of such particular benefit, grant may not be conditioned on the recipient choosing such a course of study.



## Employer-Related Scholarships

**7. Other objectives:** The terms of the grant and the courses of study for which grants are available must meet all other requirements of section 117 of the Code and the regulations thereunder, and must be consistent with a disinterested purposes of enabling the recipients to obtain an education in their individual capacities solely for their personal benefit and must not include any commitments, understandings or obligations, conditional or unconditional, suggesting that the studies are undertaken for the benefit or to accomplish any purpose of the employer or the foundation.



# Employer-Related Scholarships

## Percentage Test

**For Grants to Children of Employees:** Number of grants awarded in any year may not exceed:

- 25% of the number of employees' children who, (i) were eligible, (ii) were applicants for such grants, and (iii) were considered by the selection committee in selecting the recipients of grants in that year, **OR**
- 10% of the number of employees children who can be shown to be eligible for grants in that year (whether or not they submitted an application).

**For Grants to Employees:** Number of grants awarded in any year may not exceed:

- 10% of the number of employees who, (i) were eligible, (ii) were applicants for such grants, and (iii) were considered by the selection committee in selecting the recipients of grants in that year.





# Employer-Related Scholarships

## **Employer-Related Scholarship Funds Held by Community Foundations**

The Council has long taken the position that, although Rev. Proc. 76-47 applies only to grant programs at private foundations, public charities that administer employer-related scholarship funds (such as community foundations) should follow the same guidelines.



## Employer-Sponsored Assistance Programs

- Grants may be paid to assist employees dealing with the consequences of a disaster or personal hardship.
- May come from a private employer-related foundation or a fund established by the employer at a public charity.
- Subject to certain restrictions to ensure that assistance to the employee does not result in an impermissible private benefit to the employer.
- Not intended to cover hardship due to a loss or reduction in employment, poor management of personal finances, losses that would be covered by insurance (and should not be treated by employees as a substitute for insurance), etc.
- May not be used to induce employees to follow a course of action sought by the employer or designed to relieve the employer of a legal obligation for employee benefits.



# Employer-Sponsored Assistance Programs

## **Qualified Disaster Relief (IRC § 139)**

A “qualified disaster” includes:

- A disaster resulting from certain terrorist or military actions
- A Presidentially declared disaster
- A disaster resulting from an accident involving a common carrier
- Any other event the Secretary of the Treasury determines is catastrophic

Payments from a private employer-sponsored foundation to employees or their family members may be made to provide relief from a “qualified disaster” and will not constitute an act of self-dealing or result in taxable compensation to the employee if:

- The class of beneficiaries is large or indefinite
- Recipients are selected based on objective determinations of need
- Selection is made using either an independent selection committee or adequate substitute procedures to ensure that any benefit to the employer is incidental and tenuous.
  - “Independent” means a majority of committee members are not in a position to exercise substantial influence over affairs of the employer.



# Employer-Sponsored Assistance Programs

## **Qualified Disaster Relief (IRC § 139)**

Qualified disaster relief payments can include:

- Reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster,
- Reasonable and necessary expenses incurred for the repair or rehabilitation of a personal residence due to qualified disaster (need not be owned – can also apply to rentals)
- Reasonable and necessary expenses incurred for the repair or replacement of the contents of a personal residence due to qualified disaster.

Relief must be based on an objective evaluation of the individual's needs at the time the grant is made, not merely because an individual is a victim of a disaster.



# Employer-Sponsored Assistance Programs

## **Disaster Relief from Public Charities**

- Generally preferable to employee relief from an employer-related private foundation.
- Many employers choose to partner with local community foundations or dedicated disaster relief public charities to house their employee relief funds.
- Not limited to just qualified disaster relief – a public charity may provide broader kinds of relief (e.g., personal hardship resulting from illness or a house fire).
- Having a third-party public charity administer an employer-sponsored assistance program ensures an independent review and takes advantage of that public charity's expertise in administering such funds.



# Questions?



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