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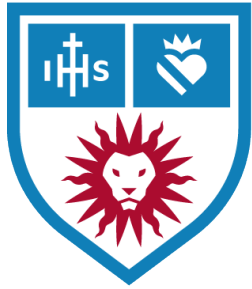
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Standards for Charitable Disaster
Relief In the Time of Pandemic

Professor Ellen P. Aprill

Standards for Charitable Disaster Relief In the Time of Pandemic

by Ellen P. Aprill



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In this article, Aprill argues that the standards established for disaster relief set forth in the Victims of Terrorism Tax Relief Act of 2001 are well matched to the COVID-19 crisis, and that disaster relief organizations need assurance and guidance that their decisions regarding need for aid will not later be subject to scrutiny or question.

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The IRS's announced rules for charities offering disaster relief, including charities responding to the COVID-19 crisis, are detailed and onerous. These rules are also long-standing. The IRS applied them in connection with the Oklahoma City bombing 25 years ago. Their invocation after the September 11, 2001, terrorist attacks, however, prompted an enormous outcry. In response, the IRS changed its position and shortly thereafter, Congress codified those changes.¹ The legislation, however, applied only to charities responding to the September 11

attacks and some anthrax attacks. Language from the Joint Committee on Taxation states that the more generous September 11 rules should also apply to any qualified disaster, but no IRS document has taken this position. Congress could do as it did in 2001 and reenact the September 11 rules for disaster relief, at least for the COVID-19 pandemic, if not for all disasters defined in section 139(c) or 165(h)(3)(C)(1). If Congress does not quickly do so, the IRS can and should.

The IRS rules for charitable organizations offering disaster relief can be found only in the IRS's disaster relief publication,² and not in any document published in the Internal Revenue Bulletin. These rules revert to pre-September 11 standards; to qualify as a disaster relief charity, organizations must benefit an indefinite, open-ended group of beneficiaries, known as a charitable class, and make detailed individualized determinations of need.

The IRS has never defined charitable class precisely. The disaster relief publication states:

A charitable class must be large enough or sufficiently indefinite that the community as a whole, rather than a pre-selected group of people, benefits when a charity provides assistance. For example, a charitable class could consist of all the individuals in a city, county or state. This charitable class is large enough that the potential beneficiaries cannot be individually identified and providing benefits to this group would benefit the entire community.

The publication further explains that "a tax-exempt disaster relief or emergency hardship

¹These developments are discussed in more detail in Ellen P. Aprill, "Charitable Class, Disaster Relief, and First Responders," *Tax Notes*, Nov. 14, 2016, p. 949. This piece borrows from that article at various points. See also Aprill and Richard L. Schmalbeck, "Post-Disaster Tax Legislation: A Series of Unfortunate Events," 56 *Duke L.J.* 51-100 (2006).

²IRS Publication 3833, "Disaster Relief: Providing Assistance Through Charitable Organizations" (rev. Dec. 2014).

organization cannot target and limit its assistance to specific individuals, such as a few persons injured in a particular fire.”³ According to the publication, victims of a single hurricane can constitute a charitable class when more than 100,000 homes are damaged because “the disaster is large enough that providing aid to this group benefits the public as a whole.”⁴ The publication gives guidance neither as to when groups larger than a few and less than a 100,000 constitute a charitable class, nor whether these standards for charitable class apply only for disaster relief generally or to all charitable organizations.

Perhaps even more importantly for the COVID-19 pandemic, the disaster relief publication asserts, “Generally, a disaster relief or emergency hardship must make a specific assessment that a recipient of aid is financially or otherwise in need.”⁵ Also, “Charities must also maintain appropriate records to show that they have made distributions to individuals after making appropriate needs assessment based on the recipients’ financial resources and their physical, mental and emotional well being.” The publication lists nine different factors that must be documented, including description of the aid, cost of the aid, selection criteria, and purpose of the aid. In this time of shelter in place and restricted gathering, among many other challenges, disaster relief organizations will find it particularly difficult to satisfy these requirements. The publication does not state any special rules for charities assessing need in a qualified disaster.

Charities need guidance for this pandemic — guidance in a form on which they can rely. Either the IRS or Congress can provide it. Both did so after the September 11 terrorist attacks. On November 8, 2001, a heated congressional hearing focused on the difficulties with the IRS applying the usual disaster relief requirements

to this crisis.⁶ The IRS quickly backtracked. On December 10, 2001, explicitly anticipating legislation, the IRS issued Notice 2001-78, 2001-2 C.B. 576, stating that payments made by a charity to individuals or their families because of the terrorist attacks would be treated “as related to the charity’s exempt purpose provided that the payments are made in good faith using objective standards.”⁷ Then-IRS Commissioner Charles O. Rossotti explained that the notice sent a “clear signal” to charities that organizations acting “in a reasonable, good-faith manner to get help to victims will not endanger their tax-exempt status.”⁸

Congress followed up. Not long after the IRS notice, it enacted the Victims of Terrorism Tax Relief Act of 2001 (VTTRA).⁹ This legislation permitted charities responding to that disaster and to some anthrax attacks to make only a “good faith” determination of need “using a reasonable and objective formula which is consistently applied,” rather than an individualized determination of need. As the JCT explained, VTTRA relieved charities from the requirement “to make a specific assessment” of need before disbursing funds.¹⁰ VTTRA, however, did not change the required determination of need for charities responding to other disasters, including our current one.

VTTRA also added section 139 to the code. This provision excludes from gross income payments to or for the benefit of individuals “to reimburse or pay reasonable and necessary personal, family, living or funeral expenses incurred as a result of a qualified disaster.”

⁶ Hearing on Charitable Organizations Providing September 11th Disaster Relief Before House Ways and Means Subcommittee on Oversight (Nov. 8, 2001) (testimony of Steven Miller, Director, IRS Exempt Organizations, Tax-Exempt/Government Entities Division (Nov. 9, 2001)).

⁷ Notice 2001-78.

⁸ *Id.*

⁹ P.L. 107-134, 115 Stat. 2427. Congress passed VTTRA on December 20, 2001, and President Bush signed VTTRA on January 23, 2002.

¹⁰ JCT, “Technical Explanation of the ‘Victims of Terrorism Tax Relief Act of 2001’ as Passed by the House and the Senate on Dec. 20, 2001,” JCX-93-01, at 11, 17-18 (Dec. 21, 2001).

³ *Id.*

⁴ *Id.*

⁵ *Id.*

Qualified disasters include those resulting from a terroristic or military action, disasters declared by the president, or those declared by the Treasury secretary.¹¹

The JCT treated its explanation of section 139 as a springboard for a discussion of exemption concerning disaster relief for both public charities and private foundations. Recognizing that the legislation addressed only the September 11 attacks and some anthrax attacks, it stated the following about disaster relief generally¹²:

Charitable organizations generally are in the best position to determine the type and amount of, and appropriate beneficiaries for, disaster relief. Accordingly, it is expected that the Secretary will presume that a charity providing cash assistance in good faith to victims (and their family members) of a qualified disaster is acting consistent with the requirements of section 501(c)(3) if the class of beneficiaries is sufficiently large or indefinite and the charity can demonstrate that it is applying consistent, objective criteria for assessing need.

But no IRB document confirms this JCT expectation. Moreover, nowhere does the disaster relief publication adopt this position.

The JCT explanation of section 139 also considered disaster relief provided to employees by private foundations controlled by their employers. It rejected several IRS private letter rulings involving employer-sponsored foundations and concluded that “an employer-controlled private foundation is not providing an inappropriate benefit and is not disqualified from exemption under section 501(c)(3)” by making payments to company employees who are victims of a qualified disaster as defined under newly enacted section 139.¹³ It directed the IRS “to issue prompt guidance to taxpayers relating to the

requirements applicable to private foundations making disaster assistance payments.”¹⁴

In contrast to the JCT direction regarding charitable needs assessment, the IRS heeded this command. The disaster relief publication sets forth rules regarding aid from private foundations to employees as specified by the JCT.¹⁵ The IRS also has issued more official guidance regarding disaster relief from employers to employees. Under the authority granted to the secretary under section 4966(d)(2)(C), Notice 2006-109, 2006-2 C.B. 1121, exempts from the definition of donor advised fund and thus from excise taxes under section 4966 employer disaster relief funds. The exception applies to employer funds housed at a community foundation or other public charity that an employer has established to provide disaster relief grants to employees or their family members who are the victims of a major disaster. The notice lists several other requirements:

- the fund must serve a single identified charitable purpose, which is to provide relief from one or more qualified disasters within the meaning of section 139;
- the fund must serve a large or indefinite class (a “charitable class”);
- recipients of grants from the fund must be selected based on objective determinations of need;
- the selection of recipients of grants from the fund must be made using either an independent selection committee or adequate substitute procedures to ensure that any benefit to the employer is incidental and tenuous;¹⁶ and
- no payment can be made from the fund to or for the benefit of any director, officer, or trustee of the sponsoring organization of the fund, or members of the fund’s selection committee.

¹¹ Section 139(c). More specifically, when the cross-references in section 139(c) are consulted, qualified disasters include terrorist or military action or a threat of military action directed against the United States or its allies; military action involving the U.S. Armed Forces resulting from violence against the United States or its allies; a disaster declared by the president that triggers assistance from the Federal Emergency Management Agency; or a disaster determined by the secretary.

¹² JCT, *supra* note 10.

¹³ *Id.*

¹⁴ *Id.*

¹⁵ It does so somewhat reluctantly, noting the IRS had taken previously ruled differently, but that the publication was adopting the position Congress articulated after the September 11 attacks. IRS publication, *supra* note 2.

¹⁶ The 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. *Id.*

The fund must also maintain adequate records that demonstrate the recipients' needs for the disaster relief assistance provided.

As a result of President Trump's letter of March 13, 2020, declaring the COVID-19 crisis to constitute an emergency under the Stafford Act, this pandemic qualifies as a section 139 qualified disaster.¹⁷ Many law firms have issued memoranda reminding employers of the ability to use this special donor-advised fund (DAF) exception and other ways to use section 139 to help their employees.¹⁸

The DAF exception in Notice 2006-109, however, speaks only of an employer relief fund established for that employer's employees. It does not extend, for example, to situations across the country currently raising enormous concerns — such as needy students at colleges and universities¹⁹ or independent contractors and employees of other entities that serve other employers by contract, such as security firms or food service providers. For charities to help such individuals, IRS guidance states that they must meet the onerous requirement of individualized determination of need generally applicable to disaster relief organizations.

This state of affairs seems puzzling, if not wrongheaded. Employers can benefit their employees in a way once deemed to constitute impermissible benefit by using the simplified procedures identical to those that VTTRA established for September 11 disaster relief charities. In contrast, it appears that the IRS expects COVID-19 disaster relief charities to make individualized determinations of need.

¹⁷ As explained in *supra* note 11, section 139(c)(2) cross-references to section 165(h)(3)(C)(1), which in turn defines "federally declared disaster" to include any that the president of the United States determines to warrant assistance under the Robert T. Stafford Disaster Relief and Emergency Assistance Amendments of 1988.

¹⁸ I note that the section 139 income exception also explicitly applies to payments from governmental entities under section 139(a)(4).

¹⁹ In FAQs issued on May 6, 2020, the IRS indicated that any emergency financial aid funds authorized by the CARES Act (P.L. 116-136) that undergraduate and graduate students receive under the Higher Education Act for unexpected expenses as a result of the COVID-19 pandemic will be excluded from income under section 139. Like IRS publications and JCT legislative history, however, taxpayers cannot rely on FAQs, which are not published in the IRB.

Congress may well enact additional COVID-19 legislation. In any such legislation, it could remedy this inconsistency in connection with disaster relief by at least allowing the charities offering COVID-19 relief to adopt the same standards given to charities in connection with the September 11 attacks.

But the IRS can and should act on its own. The latest guidance regarding disaster relief charities is embodied only in a publication, not in a document published in the IRB. In 2001 the IRS issued a notice changing its position regarding standards for September 11 disaster relief organizations. It should do so again for the COVID-19 pandemic.

A requirement of "consistent, objective criteria for assessing need" rather than an individualized assessment of needs is especially appropriate for this pandemic. Worries expressed after VTTRA about use of its charitable needs standard as a dangerous precedent do not apply to this pandemic. Some were troubled that VTTRA contorted the dimensions of charitable law by having charities operate as a tort compensation fund. For example, Laurie Slutsky, then-president of the New York Community Trust, the country's largest community foundation, wrote that victim compensation differs from the goals of charity. "Victim compensation is about monetizing the value of a lost breadwinner and making sure that a family is provided for, while charity seeks to find ways to provide emergency relief and services that help people to move beyond a very painful or traumatic event in their lives to a point where they can start to rebuild their lives."²⁰

Robert Katz expressed similar concerns. To him, VTTRA "essentially waived" the prohibition against private benefit for organizations engaged in September 11 relief. "It freed such entities to make payments without regard to actual need."²¹ Katz tracked the results of those special rules. The Twin Towers Fund, he reports, raised at least

²⁰ Lorie Slutsky, "Perspectives," at 113-114 (2002). Others have also noted the pressure on organizations in the face of a disaster to move from dispensing charitable relief to acting as a tort fund. See also Robert A. Katz, "A Pig in a Python: How the Charitable Response to September 11 Overwhelmed the Law of Disaster Relief," 36 *Ind. L. Rev.* 251, 271 (2003).

²¹ Katz, *supra* note 20, at 331.

\$440,640 for each of the 438 uniformed and other official personnel killed at the World Trade Center, and the New York Firefighters 9-11 Disaster Relief Fund raised at least \$418,000 for each of the 347 fire department personnel killed at the World Trade Center.²² Katz finds these sums “legally excessive” under common law.²³

The enormous need arising out of the COVID-19 pandemic overwhelms concerns about excessive grants. For example, in his April 19 State of the City report, Eric Garcetti, the mayor of my hometown of Los Angeles, described the entire city as under attack.²⁴ *The Washington Post* recently reported that 22 million Americans have filed for unemployment.²⁵ *The New York Times* on April 20 estimated the number of total coronavirus cases in the United States as 753,317²⁶ and the number worldwide has been reported as just under 2.5 million.²⁷ Thus, the concerns that followed VTTRA seem unlikely to emerge in connection with this pandemic.

The standards established for disaster relief set forth for the September 11 attacks in VTTRA are well matched to the latest crisis. Congress or the IRS should help charities to address our country’s — and the world’s — desperate needs in light of the COVID-19 pandemic. Disaster relief organizations need assurance that their decisions regarding need for aid will not later be subject to scrutiny or question. They require guidance that is more official and more certain than contradictory statements in a JCT explanation and an IRS publication. ■

²² *Id.* at 255.

²³ *Id.* at 254.

²⁴ David Zahniser, Dakota Smith, and Emily Alpert Reyes, “Garcetti: L.A. Is ‘Under Attack’ and Will Need to Furlough Thousands of City Workers,” *The Los Angeles Times*, Apr. 19, 2020.

²⁵ Heather Long, “U.S. Now Has 22 Million Unemployed, Wiping Out a Decade of Job Gains,” *The Washington Post*, Apr. 16, 2020.

²⁶ *The New York Times*, “Coronavirus in the U.S.: The Latest Map and Case Count.”

²⁷ Worldometer.com, “COVID-19 Coronavirus Pandemic.”

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