



Tax-Free Disaster Relief Payments Under Internal Revenue Code Section 139

As the nation responds to COVID-19 and a world pandemic, IRC §139 may be one more tool in an employer's toolkit to help their employees with fighting this silent war.

Under the Internal Revenue Code ("IRC") §139(a), a "qualifying disaster relief payment" from an employer to an employee is excluded from gross income, the opposite of normal tax law.

IRC §139 applies after the President of the United States declares a disaster. On March 13, 2020, President Trump made an emergency declaration under the Robert T. Stafford Act, evoking the protections of §139.

Importantly, an employer that provides a qualifying disaster relief payment is not required to include those amounts as wages (or as self-employment earnings) under IRC §139(d). Therefore, these employer payments to employees are income and employment tax-free for federal tax purposes, and the employer is entitled to a tax deduction for the payment as a business expense.

The practical aspects of how §139 can help employees is based on the relevant question, "what constitutes a qualified disaster relief payment relating to the COVID-19 pandemic?"

The answer is a payment to an individual "to reimburse or pay reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster," provided the amount is not reimbursed by insurance or otherwise, such as governmental assistance. Further, the expense cannot reimburse for lost wages or replace lost business income.

As the expense must be "incurred as a result of" the COVID-19 pandemic, whether any particular payment is a qualifying disaster relief payment will be a factual determination. It is important that any reimbursements are backed up with documentation, and obtaining outside experts to assist you in that determination is important for establishing a reasonable basis for your tax position.

The legal standard is whether expenses are incurred as a result of the disaster. For example, if an employee is teleworking and must incur new expenses, including childcare, necessary equipment, and increased utility expenses, a good argument can be made that these type of expenses should meet the qualifying disaster relief definition.

IRC §139 was added in 2001 by the Terrorism Tax Relief Act. Although the legislative history to §139 provides that "in light of the extraordinary circumstances surrounding a qualified disaster, it is anticipated that individuals will not be required to account for actual expenses in order to qualify for the exclusion," IRS guidance indicates that an employer reimbursement program should contain requirements ensuring the reimbursed amounts were reasonably expected to be commensurate with unreimbursed disaster relief payments.

Good documentation is always important, and employers are encouraged to use their standard accountable reimbursement program as a model to document any payments made to an employee. An employer's reimbursement program generally should have a plan that is drafted with rules and assist the employer from creating discriminatory issues or other employment related legal issues. Although employers are not required to have employees document actual expenses, we recommend you make every effort to obtain documentation. If documentation cannot be obtained, employers should require signed statements from employees affirming that their claims qualify with the requirements of

Additional COVID-19 resources from Chamberlain Hrdlicka are available at this link:
https://www.chamberlainlaw.com/practices-chamberlain_covid-19_resources.html

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