Employers Can Provide Tax-Free Assistance to Employees Impacted by COVID-19

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Code section 139 excludes from taxable income "qualified disaster relief payments" made to reimburse or pay reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a "qualified disaster" provided the amounts are not covered by insurance or otherwise. Section 139 can be used by any organization, including employers that want to help employees and their families impacted by the global response to COVID-19. Employers are not required to have their employees substantiate paid or reimbursed expenses as long as the amount of the payments is reasonably expected to be commensurate with the expenses incurred.

A qualified disaster includes any "presidentially-declared disaster," which is a disaster determined by the President of the United States to warrant assistance by the federal government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act (the "Stafford Act"). President Trump issued a declaration of emergency under 501(b) of the Stafford Act in his letter dated March 13, 2020. Although the definition of "presidentially-declared disaster" does not expressly include presidentially-declared "emergencies," the IRS has affirmatively stated its belief in Revenue Ruling 2001-15 that for purposes of the definition, disaster includes an event that is declared an "emergency" under the Stafford Act. In addition, IRS Notice 2020-18 treats the president's emergency declaration as a presidentially-declared disaster for purposes of extending the federal income tax filing and payment deadline for taxpayers with an April 15, 2020 due date.

Employers intending to make qualified disaster relief payments need to be mindful that only reasonable and necessary expenses actually incurred by employees as a result of COVID-19 can be reimbursed or paid. Because most disasters warranting assistance under section 139 are natural disasters, there is little to no guidance on what types of expenses can be covered in connection with a

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global health crisis. Guidance from the IRS addressing what expenses are eligible under section 139 would be welcome.

Employers may wish to assist current or former employees who are experiencing a reduction in hours or job loss with regular housing payments and food costs, but the legislative history of section 139 makes clear that qualified disaster relief payments cannot be in the nature of income replacement, such as lost wages or unemployment compensation, so paying housing and food costs that would be incurred even without the Coronavirus situation can't be paid tax-free under 139. On the other hand, medical expenses incurred as a result of contracting COVID-19 would clearly be incurred as a result of the virus, but only to the extent they are not covered by insurance. It seems reasonable that unexpected childcare costs and the cost of temporary housing, if an employee is unable to remain in his or her home due to the need to quarantine, should qualify as reasonable and necessary expenses incurred as a result of COVID-19.

We recommend that employers adopt a written plan outlining when employees are eligible for qualified disaster relief payments and what qualifies as reimbursable expenses. A written application should also be adopted as part of an employer's program and provided to employees to apply for assistance. While employees are not required under section 139 to substantiate their expenses, an employer should require employees to certify on the written application that any assistance payments will only reimburse expenses that are reasonable and necessary. Employers should also consider forming a committee to review employee applications for assistance and administer the program.

Qualified disaster relief payments are not subject to federal income tax or employment tax withholding and do not need to be reported on an employee's Form W-2. Section 139 payments are also deductible by the employer under section 162 as ordinary and necessary business expenses.

For more information please contact Alison Stemler, Scott Dolson , or any attorney in Frost Brown Todd's Employee Benefits or Tax practice groups. For up to date information on tax-related issues, visit the Tax Law Defined Blog.

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To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Response Team. Our attorneys are on hand to answer your questions and provide guidance on how to proactively prepare for and manage any coronavirus-related threats to your business operations and workforce.

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