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Employers may make tax-free qualified disaster relief payments to employees to reimburse or pay certain reasonable and necessary expenses incurred by the employee in connection with the COVID-19 pandemic. Below you will find information on the taxation, use, amount and substantiation of these payments.

## Taxation

In general, amounts provided by employers to employees are taxable to those employees. However, Internal Revenue Code Section 139 provides an exception for “qualified disaster relief payments,” generally available when there is a federally declared disaster. The IRS interpreted the President’s March 13, 2020 declaration under the Robert T. Stafford Relief and Emergency Act with respect to the COVID-19 pandemic as constituting such a federally declared disaster.

Qualified disaster relief payments are excluded from gross income and from wages and compensation for purposes of employment taxes. Thus, they are not subject to income tax withholding, FICA, or FUTA, do not have to be reported by an employer making the payment on the receiving employee’s

Form W-2, and do not have to be reported as income by the affected employee. The payments are also nontaxable in most, but not all, states. The employer deducts the payments as wages.

## What Can These Payments be Used For?

Qualified disaster relief payments may be used to pay or reimburse reasonable and necessary personal, family, living, or funeral expenses as incurred as a result of a qualified disaster. What this may be in light of COVID-19 is not specifically addressed, but basic necessities such as food, shelter, childcare, telecommuting, and medical expenses would likely qualify. Code Sec. 139 qualified payments do not include any amounts intended as wage replacement and amounts that were not incurred with respect to the declared disaster. There can be no “double dipping” (i.e., the expense cannot otherwise be compensated by insurance or otherwise – FFCRA paid leave will not also qualify under Code Sec. 139).

## Amount of Payments

There is no IRS limit. Payments can vary by employee and there are no applicable nondiscrimination rules.

## Substantiation

The IRS has informally indicated that recipients are not required to account for actual disaster relief payments in order to qualify for the Code Sec. 139 exclusion, provided that the amount of the payment can be reasonably expected to be commensurate with the expense incurred. It is uncertain whether individuals receiving payments may later be called upon to demonstrate that the expenses for which they received disaster relief payments were not subject to reimbursement through insurance or otherwise.

## Employer Action

Qualified disaster payments were first instituted following 9/11. There is little guidance concerning them and there is no guidance specifically addressing Code Sec. 139 as it relates to COVID-19. Employers who wish to make qualified disaster payments should review Code Sec. 139 and consult with a CPA or other tax advisor with any questions.

