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## Can Employers Use Code Section 139 to Help Employees in the Coronavirus Pandemic?

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Businesses and individuals are trying to cope with the coronavirus pandemic and the effects that it is having on the economy and society. President Trump has declared a national emergency and several relief bills have been enacted. Some employers, if they are in a position to do so, may be looking to provide additional help to their employees. But can that be done in a tax efficient manner? The answer may be yes, thanks to Internal Revenue Code Section 139. If Section 139's requirements are met, employers can make grants to employees that won't be treated as wages or be taxable to employees.

Section 139 excludes from an individual's taxable income a "qualified disaster relief payment." This includes, among other items, amounts to reimburse or pay "reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster." Once President Trump designated the pandemic as a nationwide emergency, it opened up the possibility to use Section 139.

The only official guidance that the IRS has issued on Section 139 is Revenue Ruling 2003-12 in which the IRS ruled that an employer that made grants to its employees who were affected by a flood in a presidentially declared disaster area could treat those amounts as qualified disaster relief payments. The employer set up a written program to establish and administer the grants to its employees, and the ruling provides a roadmap for employers who wish to set up a Section 139 program.

The situation we're facing now is different from the typical scenario where Section 139 would be utilized. Usually, Section 139 is applied in the context of a natural disaster in which property needs to be repaired or replaced, or people need to find temporary housing while they are unable to use their residences. All of

those types of expenses are clearly covered by Section 139. The coronavirus and its fallout are causing different types of economic damages, including increased medical and child care expenses as a result of schools being closed. The closures and slowdowns of certain businesses have resulted in lost or reduced income, but it appears to be difficult to classify lost income as an expense that can be reimbursed under Section 139 because it is not an expense, but lost income. Additionally, normal living expenses (such as mortgage payments, utilities, or food) probably don't qualify under Section 139 because those expenses arise normally and are not incurred as a result of the disaster. However, to the extent that an individual incurs additional reasonable and necessary personal, family, or living expenses as a result of the disaster, they would qualify under Section 139. It's also important to remember that Section 139 doesn't apply to any expenses that are reimbursed, such as by insurance.

If an employer is interested in setting up a Section 139 program, it needs to adopt a plan document to govern it, much like the employer has to adopt a 401(k) plan document. The good news is that the plan document doesn't need to be long (just a few pages), but it does need to specify a few details about how the program will work. Using guidance from the program that was described in Rev. Rul. 2003-12, an employer's program should specify the following:

- The disaster to which it relates and the employees who are eligible to receive grants.
- The types of expenses that may be covered by payments from the program.
- Language stating that payments cannot be used to reimburse the cost of nonessential, luxury, or decorative items and services.
- Rules for the administration of the program, including giving the administrator the authority to make discretionary decisions.
- If desired, a per-employee maximum on grants.
- An end date by which applications for grants under the program must be submitted.

## Client Alert

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Once the program is in place, it's also good practice (although not a technical requirement) to develop an application form that an employee would need to complete in order to receive a grant under the program. In the application, the employee should be required to state the amount he or she is requesting and to represent that the request does not exceed the amount of the employee's unreimbursed reasonable and necessary expenses, and that the grant will be used for qualifying purposes and not for non-essential, luxury, or decorative items and services. This requires the employee to represent that he or she did in fact incur expenses for which Section 139 can apply. Although the program described in Rev. Rul. 2003-12 did not require employees to provide evidence of the expenses, the employer could do that if desired.

If the grants under the program qualify under Section 139, the tax results are good for both the employer and the employee. Employers get to deduct the payments as a business expense, but since the payments aren't treated as wages, the employer isn't required to pay FICA taxes on the grants. Employees aren't required to include the grants as income for income taxes, and also don't have to pay FICA taxes. The grants won't appear on the employee's W-2 for the year of the grant.

Employers who are aware of their employees incurring additional expenses as a result of the virus can consider using a Section 139 program to help employees with those expenses. Establishing a Section 139 program is not difficult and would greatly assist employees in a time of need. Shumaker's attorneys can assist with drafting the appropriate program documents to ensure compliance with Section 139.

For the most up-to-date legal and legislative information related to the coronavirus pandemic, please visit our Shumaker COVID-19 Client Resource Center at [shumaker.com](https://shumaker.com). We have also established a 24/7 Legal & Legislative Helpline at 1.800.427.1493 monitored by Shumaker lawyers around the clock.

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