



COVID-19 Crisis and Code Section 139 Tax-Free Disaster Assistance to Employees and Contractors

April 2020

In the ordinary course, employers can provide tax-free reimbursement of reasonable business expenses that employees incur working from home, such as home office supplies and added utility costs, under Code section 162. Some states and districts – such as CA, IL, and DC – may even require reimbursement of these expenses.

The March 13, 2020 presidential emergency declaration on COVID-19 also enables employers to provide tax-free payments for unreimbursed “personal, family, living or funeral expenses” associated with the pandemic, under Code section 139.

According to the legislative history for Code section 139, such payments cannot cover lost wages – which means they can’t be used to cover a new paid leave program. However, tax-free payments might be used to compensate employees for other “reasonable and necessary” expenses due to the COVID-19 emergency. Unlike an ordinary and necessary business expense under Code section 162, a disaster-related payment under section 139 does not require that employees substantiate their expenses, so long as the payments reasonably approximate the costs. Nondiscrimination rules under Code section 105(h) do not appear to apply.

Examples of Expense Reimbursements that Should be Permissible

IRS guidance might be helpful to understand how broadly to read Code section 139, but we think many types of expenses should be reimbursable on a tax-free basis:

For Those Continuing to Work On-Site

- New childcare costs resulting from school or daycare closings, or absence of normal caretaker
- Added personal costs to continue working and living safely (e.g., disinfectants, PPE, temporary accommodations away from family members who are ill or higher risk)
- Added costs of safely commuting (although consider whether deduction disallowance applies under Section 274(a)(4) and Section 274(l))

For Those Sheltering

- Cost of delivery for food or other essentials (although generally not the cost of food that would otherwise be consumed)
- Cost of additional supplies and essentials (e.g., stocking up on canned goods, disinfectant, and medicine)
- Added living costs due to college students returning home (e.g., food or other essentials)
- Technology to facilitate distance learning (e.g., tablet, necessary software, homeschooling materials)

- Technology to facilitate communication with family and relatives (e.g., increased phone, data, shipping costs; Facebook Portal or tablet for seniors)

For Those Ill or Caring for the Ill

- Special living expenditures due to quarantine (e.g., disinfectants, PPE, other supplies)
- Non-reimbursed or non-prescribed medical supplies (heart rate monitor, blood oxygen monitor)
- Personal travel costs (gas or air travel, lodging) to take care of a sick or quarantined family member

*Note: to the extent the reimbursement covers medical expenses, ERISA and other considerations.

Mobile Workforce (e.g., Expatriates)

- Travel costs of unexpected repatriation or relocation for self and family
- Living costs in area to which individual and family are repatriated
- If expatriation is delayed, temporary living costs, carrying costs for home that cannot be sold

Q: How are Section 139 Payments Reported?

Section 139 payments are tax-free to the recipient and are neither subject to income tax withholding or other employment taxes, nor reported on a Form W-2 or 1099.

Q: Can Section 139 Tax-Free Payments Be Made if Wages Are Cut Due to Reduced Schedule, Furloughs or Layoffs?

The intent is that Code section 139 payments not serve as wage replacement. However, that should not prohibit an employer from offering these payments at the same time as a wage reduction. In many cases, employers need to reduce hours and work schedules. Employers might reduce the sting of these realities by offering reimbursements under Code section 139 for specified expenses and/or up to a specified amount.

Q: Can Section 139 Tax-Free Payments be Provided to Non-Employees or Former Employees?

Yes. Code section 139 provides this exclusion for “individuals,” not just employees. If providing to non-employees, employers should ensure that payments remain deductible. Payments to former employees generally should be deductible in the same manner as payments to current employees. Payments to contractors or customers also should generally remain deductible as an ordinary and reasonable business expense. One open question is whether deduction disallowances for food, entertainment or commuting (under Code section 274) apply; however, many employers can avoid this possibility by reimbursing other expenses.

Q: Does Section 139 Limit Tax-Free Payments to Reimbursements, or Can it Apply to In-Kind Provisions?

Either. Code Section 139 allows these expenses to be provided by either reimbursement or direct payment.

Q: Who Can Make Section 139 Tax-Free Payments?

Section 139 does not restrict which entity can make tax-free payments. They can be made by employers or private foundations affiliated with the employer (subject to self-dealing and other restrictions). In some cases, voluntary employees' beneficiary associations (VEBAs) might be able to make these payments.

Q: What Are the Next Steps for Creating a Section 139 Payment Program?

If being broadly offered, employers should consider creating a written policy describing the eligible employees, eligible costs, method and timing of reimbursement. Although not specifically required by Code section 139, a written policy can address many of the questions commonly raised by employees and help ensure that the program is administered consistently and compliantly.

For questions, please contact a member of our [Benefits Team](#). For more information on benefits issues related to the pandemic, please visit our [COVID-19 Resources Page](#).