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Providing Disaster Relief Payments or Charitable Assistance to Employees During COVID-19

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Employers may provide disaster relief payments and/or charitable assistance to employees in several ways. The following includes brief descriptions of each scenario in the context of the COVID-19 pandemic and corresponding explanations of the tax consequences to employers and employees.

1. Direct Payments. If the national pandemic caused by COVID-19 is a "qualified disaster" under Internal Revenue Code section 139, employers may make disaster relief payments directly to employees without having to include those payments in the employees' taxable wages. Employers may also fully deduct these payments from their taxable income. Under section 139, qualified disaster relief payments include reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster. Although section 139 has not been implemented during a pandemic before, it is reasonable to assume that employers could make payments to or on behalf of employees to cover personal or family medical expenses not covered by insurance, costs of over-the-counter medicine, supplies needed to maintain a healthy living environment, and other personal expenses incurred as the result of the COVID-19 pandemic.

On March 13, 2020, the President declared a nationwide "emergency" due to the pandemic. However, section 139 requires that a "disaster" must be federally declared. Over the last several days the President has made specific disaster declarations to numerous states and territories, all of which are listed on the FEMA website at www.fema.gov/coronavirus. Although several states and territories have not yet received a specific disaster declaration, in Revenue Ruling 2003-12, the IRS stated that for purposes of section 165(i) (concerning the deductibility of losses attributable to a disaster) a disaster includes an event declared a major disaster or an emergency under the Robert T. Stafford Disaster Relief and Emergency Assistance Act and the IRS commented further that a determination by the President that an area warrants assistance under the Stafford Act is also relevant to section 139 (regarding the exclusion from gross income of certain qualified disaster relief payments). In addition, the IRS referenced a "Federally declared disaster" in Notice 2020-18 (authorizing an extended due date for personal income tax returns due to the COVID-19 pandemic) referring at that time to the President's

declaration of a nationwide “emergency.” Finally, in a Q&A regarding the Families First Coronavirus Response Act, the IRS expressly stated that the COVID-19 pandemic is a “federally declared disaster” and that the COVID-19 outbreak is a “qualified disaster” for purposes of section 139 the Code

It is clear that employers may make section 139 disaster relief payments to employees in locations that have received specific disaster declarations from the President and the IRS has now expressly stated that the COVID-19 pandemic is a qualified disaster for purposes of section 139, so employers may provide disaster relief to employees on a nationwide basis.

2. Employer-Sponsored Donor Advised Funds. Some charitable organizations establish funds to hold donations received from donors and permit the donors to retain advisory privileges over investment or distribution of the donated funds. Ordinarily these funds, known as donor advised funds, cannot be used to make grants to individuals. However, an exception exists for certain employer-related funds established to benefit employees and their families who are victims of certain disasters.

Such a fund must serve the single purpose of providing assistance to employees and their family members who are suffering from a “qualified disaster,” as defined in section 139. It must also meet certain other legal requirements, including a requirement that grant recipients be selected based on an objective determination of need and by an independent selection committee or using adequate substitute procedures to ensure that any benefit to the employer is incidental and tenuous.
As noted above, the COVID-19 pandemic has been federally declared to be a “disaster” in certain locations and the IRS has stated that the COVID-19 pandemic is a “qualified disaster” for purposes of section 139. Thus, donor advised funds organized exclusively to provide relief from COVID-19-related hardships may make distributions to employees nationwide who are suffering from the pandemic.

3. Employer-Sponsored Private Foundations. Following the September 11th, 2001 terrorist attacks, and subject to certain restrictions and requirements, an employer-sponsored private foundation may provide financial assistance directly to employees and their families affected by “qualified disasters,” as defined in section 139.

As noted above, the COVID-19 pandemic has been federally declared to be a disaster in certain locations and the IRS has stated that the COVID-19 pandemic is a “qualified disaster” for purposes of section 139. Thus, an employer-sponsored private foundation could provide financial assistance directly to employees and their families nationwidewhere such employees and their families been affected by the COVID-19 pandemic

The financial assistance payments can be made by the foundation to employees and their families as long as certain safeguards are in place to ensure that such assistance serves charitable purposes, rather than the business purposes of the employer. In addition, the payments can only be made to employees or their family members affected by qualified disasters, not in non-qualified disasters or in emergency hardship situations.

If these and other requirements are met, an employer-sponsored private foundation's payments in response to a qualified disaster (1) will be treated as made for its charitable purpose; (2) will not result in prohibited self-dealing merely because the recipients are employees; and (3) will not result in taxable compensation to the employees.

4. Employer-Sponsored Public Charities. Employee assistance funds that qualify as public charities may make payments to employees and their families to assist in a broad range of situations, not just "qualified disasters." As long as the employer does not exercise excessive control over the organization, an employer-sponsored public charity may establish a fund to assist employees and their family members in response to any type of disaster or hardship situation. Other requirements must be met, including that (1) the class of beneficiaries must be large or indefinite; (2) the recipients must be selected based on an objective determination of need; and (3) the recipients must be selected by an independent selection committee or adequate substitute procedures must be in place to ensure that any benefit to the employer is incidental and tenuous.

If these and other requirements are met, an employer-sponsored public charity's payments in response to a disaster or emergency hardship are presumed (1) to be made in furtherance of the organization's charitable purpose and (2) not to result in taxable compensation to the employees.

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