Forbes

Robert W. Wood
THE TAX LAWYER

August 14, 2026

Law Passes Making Many Wildfire Victim Legal Settlements Tax Free

The Senate has followed the House in passing H.R. 5366 for wildfire victim tax relief. Once signed by the President, which is expected, the legislation effectively extends the federal tax exclusion for certain federally declared wildfire recoveries. The original exclusion was passed in the Federal Disaster Tax Relief Act of 2023, often shortened to FDTRA, signed into law in December 2024. Timing under the FDTRA was key, as it only applied to qualifying payments received by December 31, 2025, so As many wildfire victims hoped for an extension.

Payment Date Was Key To Tax Exemption

Fortunately, the new legislation extends the exclusion to any qualifying payments for *wildfires* that receive a federal disaster declaration before January 1, 2027, regardless of the payment date of the relief payment. The new legislation will also give the exclusion a place in the federal tax code, Section 139M, which should increase awareness among IRS personnel, tax advisors and taxpayers.

With the new expiration date, payments received in 2027 or later can qualify for exclusion so long as they relate to a wildfire that received a federal disaster declaration before January 1, 2027. This will relieve some of the pressure on fire survivors to settle their disputes, even under otherwise unsatisfactory terms, so that their payment would be received in time for it to qualify for the exclusion.

Disaster Declaration Date Now Controls

Under new Section 139M, the key date is the date of the *disaster declaration*, not the date of payment. That means more survivors of the same wildfire will obtain the same tax treatment for their recoveries regardless of how long it takes a defendant to agree to an appropriate settlement. It turns out exactly what is a qualifying federal disaster declarations can be a surprisingly nuanced subject. Section 139M applies for all tax years starting after December 31, 2024.

For most people, that means it applies starting with their 2025 tax returns. Because the FDTRA applied to payments received before January 1, 2026, the FDTRA and Section 139M should only overlap for 2025 tax returns. For older tax years 2020 through 2024, the FDTRA with its requirements for exclusion remains the relevant law for the exclusion and its worth reviewing wildfire victims tax checklist. For 2026 and later tax returns, Section 139M will be the controlling law for the exclusion.

Other than the change in the expiration date, Section 139M is consistent with the FDTRA. The same requirements--and points of confusion--regarding the scope of the FDTRA apply to the new Section 139M. The scope of questions in the old and new law include the language suggesting that insurance payments *do not qualify* for the exclusion. Also remaining in question is the language that limits the exclusion to amounts received by individuals.

Key Tax Questions Remain

To most people's reading, that limitation means the exclusion does not apply to partnerships, LLCs taxed as partnerships, corporations (both C corporations and S corporations), LLCs taxed as corporations, or non-grantor trusts. Fire survivors and their tax professionals are still hoping for guidance from the IRS on those points, and hoping that guidance when it comes will be favorable, in the spirit of the relief law. The fact that the exclusion will now be ensconced as new Section 139M of the tax code may make that guidance more likely to be issued.

H.R. 5366 will not formally become part of the law until the President signs it. Nevertheless, the legislation has had broad bipartisan support, passing both houses with voice votes, and it is widely expected and assumed the President will sign it into law.