

Highlights of Tax Relief Provided to Taxpayers in Response to Hurricanes Katrina, Rita, and Wilma



The Internal Revenue Service is working to provide appropriate relief and assistance to victims of Hurricanes Katrina, Rita and Wilma. If you are a hurricane victim and need help with tax matters, please call 1-866-562-5227. For updates to these and other disaster tax relief provisions go to www.irs.gov



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Katrina Emergency Tax Relief Act and the Gulf Opportunity Zone Act

Seeking to provide immediate relief to the damage caused by Hurricane Katrina, Congress passed the “Katrina Emergency Tax Relief Act of 2005” (KETRA) on September 23, 2005. This legislation contained tax relief provisions specific to the Hurricane Katrina disaster, which amounted to \$6 billion in temporary tax breaks.

Shortly after enactment of KETRA, Hurricane Rita hit Southwest Louisiana and Eastern Texas and was followed by Hurricane Wilma, striking the state of Florida. In reaction to the widespread hurricane devastation of the Gulf Coast region, Congress passed the “Gulf Opportunity Zone Act of 2005” (GOZA) in December 2005. GOZA created tax incentives valued at almost \$9 billion targeting rebuilding of the Gulf Coast. In addition to KETRA and GOZA, the Internal Revenue Service (IRS) provided relief to taxpayers impacted by Hurricanes Katrina, Rita, and Wilma.

Listings of the counties and parishes eligible for individual and public assistance are available in IRS Publication 4492, *Information for Taxpayers Affected by Hurricanes Katrina, Rita and Wilma*.

Postponements

Postponed Due Dates

The IRS postponed until February 28, 2006, deadlines for certain taxpayers affected by Hurricanes Katrina, Rita, and Wilma to perform certain time-sensitive acts, such as the filing of returns, documents, and the payment of taxes, if such acts were set to occur on or after August 29, 2005, and on or before February 28, 2006.

Notice 2005-73

Notice 2005-73 postponed until February 28, 2006, deadlines for certain taxpayers affected by Hurricanes Katrina, Rita, and Wilma to perform certain time-sensitive acts, such as the filing of returns and other documents, and the payment of taxes, if such acts were set to occur on or after August 29, 2005, and on or before February 28, 2006. For additional information, including a description of who qualifies as an “affected taxpayer” entitled to a postponement until February 28, 2006, see Notice 2005-73, 2005-42 I.R.B. 723 (October 17, 2005) and IRS News Release IR-2005-112, *Hurricane Katrina* (9-28-2005).

Notice 2006-20

Due to the continued widespread devastation from Hurricane Katrina and subsequent flooding, the IRS determined that certain parishes and counties in Louisiana, Mississippi, and Alabama required additional disaster relief. Accordingly, the IRS provided an additional postponement of time until August 28, 2006 for certain affected taxpayers to perform certain time-sensitive acts. For additional information, including a description of who qualifies as an affected taxpayer entitled to a postponement until August 28, 2006, see Notice 2006-20, 2006-10 I.R.B. 560 (March 6, 2006)

Notice 2006-56

Because some affected taxpayers need additional time to complete and file individual income tax returns for 2004 and 2005, Notice 2006-56, which supplements and modifies Notice 2006-20, 2006-10 I.R.B. 560 (March 6, 2006), provides an additional postponement of time in order for certain individual taxpayers affected by Hurricane Katrina to file a 2004 or 2005 income tax return. Specifically, this Notice provides an additional postponement of time

until October 16, 2006, for affected taxpayers, as described in Notice 2006-20, with respect to the following individual income tax returns:

(1) 2004 individual income tax returns, originally due on April 15, 2005, for which taxpayers obtained an extension of time to file until October 15, 2005, and for which Notice 2006-20 postponed the due date to August 28, 2006; and

(2) 2005 individual income tax returns, originally due on April 15, 2006, for which Notice 2006-20 postponed the due date to August 28, 2006.

Thus, this Notice defines a new group of affected taxpayers, which is a subset of affected taxpayers who are eligible for the relief provided by this Notice. This additional postponement of time is not available for any other time-sensitive acts besides these two types of returns. To ensure that they receive the relief to which they are entitled, affected taxpayers should mark “Hurricane Katrina” in red ink on the top of their returns. Also, affected taxpayers may identify themselves as eligible for relief by calling the IRS Disaster Hotline at (866) 562-5227.

Additional Time For Businesses Granted

The IRS postponed the filing and payment deadlines for certain businesses to Oct. 16, 2006, which is the same deadline established earlier for certain individual income tax return filers, in consideration of the continuing impact of Hurricane Katrina. The postponement applies to taxpayers located in the designated disaster areas.

Business taxpayers in seven Louisiana parishes and three Mississippi counties will automatically qualify for this postponement. In addition, taxpayers in other locations — covering 11 Alabama counties, 31 Louisiana parishes and 48 Mississippi counties — can also obtain the filing and payment postponements by self-identifying themselves to the IRS. A complete list of the areas included in these categories is published in IRS News Release IR-2006-135 *IRS Announces Additional Postponement of Filing and Payment Deadline for Businesses in the Gulf Coast*. Taxpayers do not need to self-identify if they have

previously done so.

The postponement of time to make payments applies to tax payments, including estimated tax payments, due on or after Aug. 29, 2005, but before Oct. 16, 2006. In addition, the failure to deposit penalty will be waived for affected taxpayers who are unable to make their deposits during this time period.

The filing and payment postponement applies to individual, corporation, partnership, estate, trust, S Corporation, generation-skipping, employment and certain excise tax returns with original or extended due dates that fall on or after Aug. 29, 2005, but before Oct. 16, 2006.

Although IRS can postpone the time to file the 2004 and 2005 returns until Oct. 16, 2006, the law does not authorize the IRS to grant additional interest and failure to pay penalty relief for the 2004 tax year. Taxpayers can request that the IRS grant relief from the penalty if the failure to pay is due to reasonable cause and not due to willful neglect.

Economic Zones

Gulf Opportunity Zone

The Act provides that the terms “Gulf Opportunity Zone” and “GO Zone” mean that portion of the Hurricane Katrina disaster area determined by the President to warrant individual or individual and public assistance from the federal government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act by reason of Hurricane Katrina. The Act also provides that the term “Hurricane Katrina disaster area” means an area with respect to which a major disaster has been declared by the President before September 14, 2005.

Rita GO Zone (Limited Benefits)

The Act provides that the term “Rita GO Zone” means that portion of the Hurricane Rita disaster area determined by the President to warrant individual or individual and public assistance from the federal government. The term “Hurricane Rita disaster area” means an area with respect to which a major disaster has been declared by the President before October 6, 2005.

Wilma GO Zone (Limited Benefits)

The Act provides that the term “Wilma GO Zone” means that portion of the Hurricane Wilma disaster area determined by the President to warrant individual or individual and public assistance from the federal government. The term “Wilma disaster area” means an area with respect to which a major disaster has been declared by the President before November 14, 2005.

Katrina Emergency Tax Relief Act

Personal Casualty Loss Limitations Lifted

For individual taxpayers who suffered casualty or theft losses to property owned for personal use which are attributable to Hurricanes Katrina, Rita and Wilma, the Acts

remove certain loss limitations. Ordinarily, to figure a deduction for a casualty or theft loss of personal-use property, taxpayers must reduce the loss by \$100 and also reduce their total casualty and theft losses by 10 percent of their adjusted gross income. Only the excess over these \$100 and 10 percent limits is deductible. The Acts remove these limits for Hurricane Katrina, Rita and Wilma casualty and theft losses of personal-use property so that the entire amount of these unreimbursed losses is deductible. To qualify, a loss must arise in the Hurricane Katrina disaster area after August 24, 2005 and be attributable to Hurricane Katrina; or arise in the Hurricane Rita disaster area after September 22, 2005 and be attributable to Hurricane Rita; or arise in the Hurricane Wilma disaster area after Oct. 22, 2005 and be attributable to Hurricane Wilma. (GOZA amended to include Hurricane Rita and Wilma victims)

Safe Harbor Methods for Personal-Use property

The IRS issued Revenue Procedure 2006-32 to assist Hurricane Katrina, Rita and Wilma victims claiming casualty and theft losses on their individual income tax returns. The guidance provides information on several safe harbor methods that individual taxpayers may use in determining their casualty and theft loss deductions under section 165 of the Internal Revenue Code. The safe harbor methods apply to personal-use residential real property and certain personal belongings damaged or destroyed as a result of Hurricanes Katrina, Rita or Wilma. The revenue procedure provides three safe harbor methods that individuals may use to determine the decrease in fair market value of personal-use residential real property. The revenue procedure also provides a fourth safe harbor method that individuals may use to determine the fair market value of certain personal belongings immediately before Hurricanes Katrina, Rita or Wilma. These safe harbor methods provide individuals, who may have lost their records, or otherwise are unable to determine proper values, with optional methods to determine the decrease in fair market value of personal use residential real property and the pre-hurricane value of certain personal belongings. However, individuals may still use the methods of determining these values described in Publication 547, *Casualties, Disasters, and Thefts*, rather than a safe harbor method.

Work Opportunity Tax Credit

The Work Opportunity Tax Credit (WOTC) provides businesses with an incentive to hire individuals from groups that have a particularly high unemployment rate or other special employment needs. The new law creates a new target group for the WOTC, “Hurricane Katrina employees.” The December 31, 2005, expiration date of the WOTC is waived for Hurricane Katrina employees. A Hurricane Katrina employee is an individual whose main home was in the core disaster area on August 28, 2005. Under the new law, employers can take the credit

for an individual hired to work in the core disaster area after August 27, 2005, and before August 28, 2007. Outside the core disaster area, employers can take the credit for a displaced individual hired after August 27, 2005, and before January 1, 2006, regardless where the employee works. The Credit amount is 25 percent of first \$6,000 in wages if employee works at least 120 hours but less than 400 hours or 40 percent of first \$6,000 in qualified wages if employee works 400 hours or more. The deduction for salaries and wages is reduced by the amount of the credit.

Employee Retention Credit

Businesses located in a disaster area that are eligible for individual and public assistance and are inoperable as a result of damage sustained by Hurricane Katrina, Rita or Wilma may claim a tax credit through the end of 2005 calendar year if they retain an eligible employee on their payroll. The tax credit equals 40 percent of the first \$6,000 of wages paid to the employee prior to January 1, 2006.

The credit is not affected if the employee reports to work at another location while the business is inoperable.

Gulf Opportunity Zone Act

Bonus Depreciation

Businesses of all sizes affected by Hurricane Katrina can take a special first year depreciation deduction for qualified property acquired and placed in service in the GO Zone after August 27, 2005, and before January 1, 2008 (before January 1, 2009 in the case of nonresidential real property and residential rental property). The special deduction is equal to 50 percent of the qualified property's depreciable basis.

Enhanced Section 179

Certain small businesses affected by Hurricane Katrina can annually deduct up to \$200,000 in qualifying property expenditures placed in service in the GO Zone. This is double the amount otherwise allowed for small business expensing. In addition, the phaseouts for level of investment increased from \$400,000 to \$1 million, allowing more small businesses to use this tax benefit. These provisions apply to qualified property acquired and placed in service in the GO Zone after August 27, 2005 and before January 1, 2008. (Plus indexing for inflation).

Clean-up and Demolition Costs

Taxpayers may choose to take a deduction for 50 percent of any qualified GO Zone clean-up costs that would otherwise be included in the basis of property. The deduction is allowed for the tax year in which the taxpayer paid or incurred the costs. Qualified GO Zone clean-up costs means amounts paid or incurred after August 27, 2005, and before January 1, 2008, for the removal of debris from, or the demolition of structures on real property located in the GO Zone that is either (a) held by the taxpayer for use in a trade or business or for the production of income, or (b) inventory or other

property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business.

Net Operating Losses

The carry-back period is extended from two to five years for net operating losses attributable to Hurricane Katrina. This provision will allow some businesses affected by the hurricane to obtain a refund of taxes paid in earlier tax years. Special carry-back rules are also provided for certain timber losses and public utility casualty losses.

Employee Housing Expenses

Up to \$600 per month is excluded from an employee's income for employer-provided housing during the period January 1, 2006 through July 1, 2006 in the region affected by Hurricane Katrina. Employers are also entitled to a tax credit for providing such housing.

GO Zone Bonds

The Act authorizes the issuance of qualified private activity bonds to finance the construction and rehabilitation of residential and nonresidential property located in the GO Zone, which includes Alabama, Louisiana, Mississippi, or any political subdivision thereof. GO Zone bonds are bonds for which 95 percent or more of the proceeds are used for qualified project costs in the GO Zone (exempt facility bonds) or that meet the requirements of a qualified mortgage issue in the zone (qualified mortgage bonds). GO Zone bonds may only be issued for projects approved by the Governor or the bond commission of the State in which the financed project shall be located. Bond proceeds may not be used to provide for country clubs, casinos, hot tub facilities, suntan facilities, liquor stores, massage parlors, golf courses, and race tracks. Bond proceeds also may not be used to finance movable fixtures and equipment. The maximum aggregate face amount of Gulf Opportunity Zone Bonds that may be issued in any State is limited to \$2,500 multiplied by the population of the respective State within the Gulf Opportunity Zone. GO Zone bonds must be issued after the date of enactment and before January 1, 2011.

New Market Tax Credits

Under the 2006 round of the New Markets Tax Credit Program (NMTC), \$600 million was allocated specifically for the redevelopment of the Hurricane Katrina GO Zone. An additional \$400 million will be allocated in 2007. The NMTC Program, established by Congress in December 2000, provides taxpayers with a credit against federal income taxes for making qualified equity investments in investment vehicles known as Community Development Entities (CDEs). Substantially all of the taxpayer's investment must be used by the CDE to make qualified investments supporting certain business activities in low-income communities.

Profiles of awards by organization names and states served are available through the Treasury Department's web page at www.cdfifund.gov.