

Congress Passes Katrina Relief Package

H.R. 3768, the Katrina Emergency Tax Relief Act of 2005 passed by Congress on September 21, 2005:

- provides business tax incentives for the affected areas,
- provides tax relief for individuals directly affected by the storm, and
- encourages charitable giving in response to the storm.

This alert outlines this legislation. We believe you may be interested in the subject matter and may have use for it yourselves or for your employees, customers, vendors or others.

Contact Info

If you would like more information, please contact any of the McKenna Long & Aldridge attorneys or public policy advisors with whom you regularly work. You may also contact:

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Please note that this is only the first tax relief package to be considered by Congress. Additional tax relief measures are expected. For example, recent reports indicate that Congress is considering enterprise zones and other tax benefits, such as capital gains tax relief, accelerated depreciation or increased expensing, and tax-exempt bond financing to attract investors to the affected areas. We will circulate follow-up alerts as developments warrant.

An upcoming McKenna Long & Aldridge *Corporate Advisory* will contain information on the Katrina Infrastructure Finance Revitalization Act (KIFRA).

I. BUSINESS INCENTIVES

- Work Opportunity Tax Credit for Hurricane Katrina Employees.
 - Temporarily creates a new target group under the Work Opportunity Tax Credit (WOTC) for Hurricane Katrina employees. This target group is comprised of individuals who, prior to the hurricane, had their principal residence in the disaster area and became unemployed as a result of Hurricane Katrina.
 - Employers located in the Hurricane Katrina disaster area may claim the WOTC with respect to Hurricane Katrina employees hired over the two year period beginning on August 28, 2005.
 - Employers located outside of this area may claim the WOTC with respect to Hurricane Katrina employees hired through the end of 2005.
 - The credit generally equals 40 percent of the first \$6,000 of wages paid to each employee in the first year (i.e., the maximum credit is \$2,400).
- Employee Retention Credit for Employers Affected by Hurricane Katrina.
 - Small employers (i.e., having an average of 200 or fewer employees in the taxable year) located in the Hurricane Katrina disaster area and

whose business is rendered inoperable as a result of damage sustained as a result of Hurricane Katrina may claim a tax credit through the end of the 2005 calendar year if they retain an eligible employee on their payroll. Eligible employees for this purpose are employees whose principal place of employment with such employer on August 28, 2005 was in the Hurricane Katrina disaster area. The tax credit equals 40 percent of the first \$6,000 of wages paid to the employee between August 28, 2005 and January 1, 2006. The credit also is allowed if the employee reports to work at another location while the business is inoperable.

II. RELIEF FOR INDIVIDUALS AFFECTED BY HURRICANE KATRINA.

- Special Look-Back Rule for Determining Earned Income.
 - Allows individuals affected by the hurricane the option of using 2004 income to calculate the child credit and the Earned Income Credit on their 2005 tax returns.
- Secretarial Authority to Make Adjustments Regarding Taxpayer and Dependency Status for Taxpayers Affected by Hurricane Katrina.
 - Grants the Treasury Department the authority to ensure that taxpayers do not lose any deduction or credit or change in filing status in 2005 and 2006 due to temporary relocations or by reason of receipt of hurricane relief.
- Exclusion for Certain Cancellations of Indebtedness for Victims of Hurricane Katrina.
 - Exempts individuals who whose principal place of abode was in the Hurricane Katrina disaster area from taxation on personal debt relief related to the hurricane, such as the cancellation of a loan secured by a mortgage on property located in the Hurricane Katrina disaster area, provided before 2007.
- Suspension of Certain Limitations on Personal Casualty Losses.
 - Waives the 10-percent and \$100 floors on deductibility of casualty losses attributable to the hurricane.
- Extension of Replacement Period for Nonrecognition of Gain.
 - Increases the reinvestment period following an involuntary conversion of property to 5 years in the case of property involuntarily converted as a result of the hurricane as long as the replacement property is located within the disaster area.
- Withdrawals and Loans from Retirement Plans for Taxpayers Affected by Hurricane Katrina.
 - Allows eligible individuals to withdraw a maximum of \$100,000 from their IRAs and pensions without paying the 10-percent penalty. Individuals eligible for the waiver may pay income tax on the distribution over three years. Income tax is not due if the distribution is repaid to the account within three years. Increases the limit on loans from pension plans from \$50,000 to \$100,000. Allows recontribution through February 28, 2006 of qualified distributions taken for home purchases that were subsequently cancelled as a result of Hurricane Katrina.
- Extension of Deadlines.
 - Extends the deadline for taxpayers affected by the hurricane for filing income, estate and gift tax returns and making income, estate and gift tax payments until February 28, 2006. Also applies this extension to excise taxes and employment taxes.

- Additional Exemption for Housing Hurricane Katrina Displaced Individuals.
 - Creates a special tax deduction for individuals who provide rent-free housing to dislocated persons for at least 60 days during the taxable year. The deduction is \$500 for each dislocated person housed in the individual's principal residence (up to a maximum of \$2,000). The deduction can be claimed in either 2005 or 2006, but cannot be claimed in both years with respect to the same person.
- Special Rules for Mortgage Revenue Bonds.
 - Waives the first-time homebuyer requirement for mortgage revenue bonds so that individuals whose homes were rendered uninhabitable by Hurricane Katrina can qualify for low-interest rate mortgages financed by these bonds through 2007. Provides that up to \$150,000 of the loan proceeds may be used to repair damaged homes. To be eligible, the home must be located in the declared disaster area or in the same state in which the mortgagor owned a principal residence located in the Hurricane Katrina disaster area and rendered uninhabitable by Hurricane Katrina.

III. INCENTIVES FOR CHARITABLE DONATIONS

- Temporary Suspension of Limitations on Charitable Contributions.
 - Individuals' cash donations to charities are exempt from the 50-percent income limitation and the phase-out of itemized deductions if the donations are made before January 2006. Corporations can be exempt from the 10-percent income limitation for cash donations if the donations are made before January 2006. In the case of a C-corporation, qualified contributions must be for relief efforts related to Hurricane Katrina.
- Increase in Standard Mileage Rate for Charitable Use of Certain Vehicles.
 - Sets the mileage reimbursement rate used to claim a deduction for the costs associated with using a personal vehicle for charitable work for the provision of relief related to Hurricane Katrina at 70 percent of the standard business mileage rate.
- Mileage Reimbursements to Charitable Volunteers Excluded from Gross Income.
 - Exempts individual volunteers from tax on reimbursements for the use of a personal vehicle for the provision of relief related to Hurricane Katrina.
- Charitable Deduction for Contributions of Food Inventories.
 - Extends the enhanced deduction for certain food donations to S-corporations, partnerships and sole proprietors through the end of the 2005 calendar year.
- Charitable Deduction for Contributions of Book Inventories.
- Allows an increased charitable deduction for C-corporations through the end of the 2005 calendar year for donations of educational books to public schools.

McKenna Long & Aldridge LLP attorneys and professionals in all practice groups are helping clients affected by Hurricane Katrina and will be working with clients seeking to rebuild the affected areas. The firm's tax group will assist clients in connection with securing tax relief and business tax incentives.

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