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Hurricane Katrina: The Response by the Internal Revenue Service

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Summary

After Hurricane Katrina, the Internal Revenue Service (IRS) announced several tax relief measures to aid affected individuals and businesses. They cover a range of subjects, from postponing deadlines for paying taxes and filing returns for individuals, employee benefit plans and tax-exempt bond issuers, to waiving penalties for certain fuel excise taxes. This report summarizes these measures and discusses the statutory authority for the IRS's actions.

The Internal Revenue Service (IRS) has announced several measures intended to provide tax relief to individuals and businesses affected by Hurricane Katrina. Many of the measures involve the IRS extending various deadlines for these taxpayers. The IRS has the authority to do so under IRC § 7508A, which allows the IRS to postpone tax-related deadlines for taxpayers affected by a presidentially-declared disaster.¹ Specifically, the IRS may extend for up to one year the deadline by which taxpayers must do certain actions, including filing returns and paying taxes (with exceptions, including returns and taxes relating to income tax withheld at source and employment taxes), filing a claim for credit or refund of any tax, and filing a petition with the tax court.² The IRS has the authority to abate interest and penalties for the period in which the deadline is

¹ The actual authority to postpone the deadlines is granted to the Secretary of the Treasury. IRC § 7508A was enacted by the Taxpayer Relief Act of 1997, P.L. 105-34. Prior to its enactment, the IRS was able to provide relief to taxpayers affected by natural disasters by extending certain tax-related deadlines dealing with the filing of returns and payment of taxes. IRC §§ 6081 and 6161. Additionally, in the event of a presidentially-declared disaster, interest was abated on the tax that was owed. Former IRC § 6404(h). As discussed in this report, IRC § 7508A provides greater authority than IRC §§ 6081 and 6161.

IRC § 7508A also applies to victims of terroristic or military actions. It is similar to IRC § 7508, which allows the IRS to postpone deadlines while a member of the Armed Forces is serving in a combat zone or contingency operation.

² See IRC § 7508(a).

extended.³ IRC § 7508A also allows the IRS to postpone the deadline by up to one year for any action required or permitted to be taken by an employee benefit plan or its sponsor, participant or beneficiary.⁴

In addition to the authority to postpone deadlines that must be met by the taxpayer, the IRS may postpone for up to one year the deadlines for certain actions it may take with respect to affected taxpayers.⁵ The IRS actions that may be postponed include assessing taxes, giving notice or demand for payment of taxes, collecting taxes, bringing suits, and allowing credits or refunds.

Taxpayers who are eligible for disaster-related deadline relief include:

- individuals whose principal residences are in the disaster area;
- businesses whose principal places of business are in the disaster area;
- relief workers assisting in the disaster area who are affiliated with government or philanthropic organizations;
- individuals, businesses, estates and trusts with necessary records that are maintained in the disaster area;
- spouses of affected taxpayers with whom they file a joint return; and
- any other person determined by the IRS to be affected by the disaster.⁶

The postponement of these various deadlines does not automatically occur when there has been a disaster. Rather, the IRS must determine whether relief is appropriate and will announce any extensions by publishing a revenue ruling, revenue procedure, notice, announcement, news release, or other guidance in the Internal Revenue Bulletin as soon as practicable after the disaster declaration.⁷ The IRS has posted its guidance related to Hurricane Katrina on its website at [<http://www.irs.gov>].

The IRS has also announced relief for taxpayers affected by Hurricane Katrina that does not involve postponing deadlines. For these actions, the report will note under each relief description where the IRS authority to take such action is found in the Internal Revenue Code (IRC).

IRS Response to Hurricane Katrina

Extended Deadlines. The IRS has extended the deadline for victims of Hurricane Katrina to file returns, pay taxes, and make tax deposits.⁸ Under the extension, any return, payment, or deposit with an original or extended due date that is after August 28, 2005,

³ IRC § 7508A(a)(2); *see also* 26 CFR 301.7508A-1(f).

⁴ IRC § 7508A(b), as amended by P.L. 107-134.

⁵ 26 CFR 301.7508A-1(b)(2).

⁶ 26 CFR § 301.7508A-1(d)(1).

⁷ 26 CFR 301.7508A-1(e).

⁸ IRS News Release IR-2005-96 (September 8, 2005); IR-2005-91 (September 2, 2005). The IRS had originally announced an extended deadline of September 15, 2005. IRS News Release IR-2005-91 (August 30, 2005).

does not have to be filed, paid, or made until January 3, 2006. During this time period, any interest and penalties assessed because of lateness will be abated.

The IRS is attempting to automatically grant the deadline extension to individuals and businesses located in the disaster area.⁹ Taxpayers located outside the area may also benefit from the deadline extension if their books, records or tax professionals are located in the area. Taxpayers seeking the relief should write “Hurricane Katrina” in red on the top of their tax forms.

IRS Actions. The IRS has also extended the deadline for actions it could take with respect to victims of Hurricane Katrina.¹⁰ If the deadline for IRS action falls on or between September 6, 2005, and January 3, 2006, the deadline has been extended to January 3, 2006. Examples of actions that the IRS may postpone include making tax assessments, issuing deficiency notices, allowing credits or refunds, collecting taxes, bringing suit, and returning property that was wrongful levied. The IRS intends to notify affected taxpayers of any postponed actions as soon as practicable.

Employee Benefit Plans. The IRS, along with the Department of Labor and Pension Benefit Guaranty Corporation, announced that employee benefit plans affected by Hurricane Katrina have been provided with an extended deadline to make minimum funding contributions or to apply for a waiver for making the contributions because of temporary substantial business hardship.¹¹ If the original deadline for making the contribution or seeking the waiver fell between August 29, 2005, and October 30, 2005, plans in the affected areas have until October 31, 2005, to make the contribution or apply for the waiver. The deadline extension applies to a plan if any of the following was located within the disaster area: the principal place of business of the plan’s sponsor or, in the case of a multiemployer plan, of the employers employing more than half of the plan’s active participants; the office of the plan or plan administrator, the office of the plan’s primary record-keeper, or the office of the enrolled actuary or other person who determines the funding requirements for the relief period.

Tax-exempt Bond Issuers. Issuers of tax-exempt bonds who are affected by Hurricane Katrina have been given an extension for certain filing and payment deadlines.¹² The relief applies to the quarterly information reporting requirements and the arbitrage filing and payment requirements. If the original deadline fell between August 29, 2005, and December 31, 2005, then the issuer has until January 3, 2006, to file the return and pay any taxes due. Penalties and interest will be abated during this time period. The IRS also stated that it would grant other types of relief to the issuers in appropriate

⁹ For a listing of counties and parishes in the disaster area, see IRS News Release IR-2005-91; see also, CRS Report RS22249, *Income Tax Relief in Times of Disaster*, by (name redacted).

¹⁰ IRS Notice 2005-66 (September 9, 2005).

¹¹ IRS News Release IR-2005-90 (September 2, 2005); IRS Notice 2005-60 (no date available).

¹² IRS News Release IR-2005-98 (September 8, 2005); IRS Announcement 2005-69 (September 9, 2005).

circumstances — for example, to issuers unable to redeem their current refunded bonds within ninety days of the refunding bonds' issue.¹³

This relief applies to issuers if any of the following is located within the disaster area: the issuer; the issuer's necessary records; the facility financed with the bond proceeds; the conduit borrower; the issuer or conduit borrower's counsel or the bond counsel for the issue; or the issuer's tax compliance professionals (such as the bond trustee, financial advisor or rebate consultant). Issuers wishing to take advantage of the deadline extension should write "Hurricane Katrina Relief. See Announcement 2005-69" in red ink on their returns.

Special Tax Assistance. The IRS has set up a toll-free telephone line for taxpayers with tax problems or questions related to Hurricane Katrina.¹⁴ The phone number is 1-866-562-5227. This line can be used to find out about tax relief and to receive Disaster Tax Loss Kits. The IRS has also announced that it, along with volunteers from the American Institute of Certified Public Accountants, will provide tax assistance at FEMA disaster recovery centers.¹⁵ The IRS does not need special statutory authority to take these actions.

Free Copies of Tax Returns. Affected taxpayers may need copies of their tax returns to apply for aid or other purposes. They can have the normal fee of \$39 waived by writing "Hurricane Katrina" in red across the top of their Form 4506 [Request for Copy of Tax Return].¹⁶ The IRS has the discretion whether to charge a fee for a copy of a return under IRC § 6103(p)(2).

Expedited Approval Process for Tax-exempt Organizations. The IRS has announced it will expedite the process for approving tax-exempt 501(c)(3) status to charitable organizations that are being set up to assist the victims of Hurricane Katrina.¹⁷ Organizations seeking the expedited process should write "Disaster Relief, Hurricane Katrina" at the top of their application form [Form 1023]. The IRS does not need special statutory authority to take this action.

Leave Donations. The IRS has also announced special treatment for employer-based leave donation programs — i.e., programs where employees donate vacation, sick or personal leave, which is then converted to cash and paid by the employer to a qualified tax-exempt organization. While the tax consequences of the donation to the employees are arguably unclear, it appears that the IRS generally takes the position that the employees must include the amount of the donated leave in their income.¹⁸ However, in response to Hurricane Katrina, the IRS has announced that contributing employees will not have to include the donations in income if the donations are made to organizations

¹³ IRS Announcement 2005-69.

¹⁴ IRS News Release IR-2005-88 (September 1, 2005).

¹⁵ IRS News Release IR-2005-94 (September 7, 2005).

¹⁶ IRS News Release IR-2005-88 (September 1, 2005).

¹⁷ IRS News Release IR-2005-93 (September 6, 2005).

¹⁸ See IRS Notices 2001-69 (November 13, 2001) and 2003-1 (January 13, 2003).

that provide relief to the victims of Hurricane Katrina and are made prior to January 1, 2007. It is not clear whether the IRC provides the authority to take this action, although the IRS took similar action after the terrorist attacks on September 11, 2001.¹⁹

Low-Income Housing Tax Credit. In order to claim the low-income housing tax credit, housing owners must rent a certain percentage of the housing to low-income individuals on a non-transient basis. The IRS has announced that it will temporarily suspend these two requirements in order to allow owners to provide housing to victims of Hurricane Katrina.²⁰ The suspension applies to any qualified low-income housing project in the United States. Thus, an owner will not be penalized if he or she rents new or vacant units to displaced victims who are not low-income individuals, and the rentals may be on a temporary basis. The housing owner must receive approval to house the individuals from the appropriate state housing credit agency. The state agency must also determine the appropriate period for which temporary housing may be provided, which may not extend beyond September 30, 2006. The IRS has stated its authority to offer such relief is found in IRC § 42(n), which reads “[t]he [Treasury] Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section [relating to the low-income housing tax credit]”

Dyed Diesel Fuel Penalty. There is a penalty tax that is assessed when dyed diesel fuel, which is generally exempt from the fuel excise taxes, is sold or used for highway use. The IRS will waive this penalty until September 15, 2005.²¹ The beginning of the waiver period differs by state: it began on August 25, 2005, in Florida, August 30, 2005, in Alabama, Louisiana, and Mississippi, and August 31, 2005, in the rest of the United States. While the waiver is applicable for any person that sells or uses the fuel for highway use, the operator of the vehicle that uses the fuel may only avoid the penalty if he or she or the fuel seller pays the excise tax of 24.4 cents per gallon. The IRS also stated that it will not assess penalties for failing to make the semimonthly deposits of the tax. Additionally, the IRS announced it will not assess the penalty on failing to meet the EPA requirements concerning highway diesel fuel sulfur so long as the EPA has waived those requirements. It appears these actions are authorized by IRC § 7508A.

Aviation Fuel Penalty. In general, aviation fuel is exempt from fuel excise taxes so long as the airport fueling terminal is secure — i.e., highway vehicles cannot remove the fuel from the terminal. The IRS will permit highway vehicles to remove aviation fuel from five airports without jeopardizing the characterization of these airport fueling terminals as being secure.²² The airports are: Louis Armstrong New Orleans International Airport, Memphis International Airport, Dallas Love Field Airport, Dallas Fort Worth International Airport, and George Bush Intercontinental Airport, Houston. The relief period is from September 2, 2005, to November 1, 2005. The IRS claims it has the

¹⁹ IRS Notice 2001-69.

²⁰ IRS News Release IR-2005-92 (September 2, 2005); IRS Notice 2005-69 (September 9, 2005).

²¹ IRS News Release IR-2005-89 (September 2, 2005).

²² IRS News Release IR-2005-95 (September 7, 2005).

authority to take this action in “exigent circumstances.”²³ This appears to refer to IRC § 4081(a)(3)(a)(iv), which reads that an airport terminal is considered secure if “except in the case of exigent circumstances identified by the Secretary in regulations, no vehicle registered for highway use is loaded with aviation-grade kerosene at such terminal.”

²³ *Id.*

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