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LEGAL TOPICS

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HURRICANE KATRINA RELIEF EFFORTS IMPACTING EMPLOYERS

Hurricane Katrina's impact has led to several efforts by federal lawmakers and agencies to provide relief. The following is a short summary of relief efforts that have particular significance for employers. Detailed rules and eligibility requirements apply to most of these programs. If you would like more information about any of these or other laws relating to disaster relief, contact us at (336) 373-8850.

Employers Can Hire Hurricane Katrina Victims Who Lack Identity and Work-Eligibility Documentation

The Department of Homeland Security ("DHS") is suspending the initiation of enforcement actions for 45 days (September 6, 2005 through October 20, 2005) for civil violations of Section 274A of the Immigration and Nationality Act with regard to individuals who are presently unable to provide identity and eligibility documents as a result of Hurricane Katrina. Normally, an employer is required to complete and retain an Employment Eligibility Verification (I-9) Form upon hiring a new employee. The I-9 Form requires verification of employment eligibility and identity through original documents provided by the employee. Recognizing the difficulty that proffering such documents may entail for Hurricane Katrina victims, DHS is instructing employers to

complete the I-9 Form, supplying as much information as possible and noting that the required documentation is not available at this time due to Hurricane Katrina. At the close of this 45-day period, DHS will revisit this suspension of sanctions and make further recommendations.

Employers Can Receive Tax Credits for Employing Hurricane Katrina Victims

Work Opportunity Tax Credit. The Work Opportunity Tax Credit, which gives employers hiring persons from certain targeted groups a tax credit of up to 40% of the first \$6,000 in wages paid to such employees (in other words, up to \$2,400 per employee), has been extended to include **Hurricane Katrina employees**. For purposes of receiving the credit, a **Hurricane Katrina employee** is a person who had his or her principal residence in the Katrina disaster area as of August 28, 2005 and either: 1) became displaced from his or her residence as a result of the hurricane, and is hired before December 15, 2005; or 2) is hired between August 28, 2005 and August 28, 2007 for a position located in the core hurricane disaster area. In other words, the tax credit provides an incentive to hire individuals who have been displaced due to the hurricane, and an incentive to resume or conduct business in the hurricane disaster area.

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Attorneys at Law

Employee Retention Credit. Employers in the Hurricane Katrina disaster area whose business became inoperable as a result of the hurricane and who employ less than 200 employees also may receive an employee retention tax credit. Similar to the work opportunity tax credit, the credit applies to 40% of the first \$6,000 in wages paid to certain employees (or up to \$2,400 per employee). In order to qualify for the credit, wages must be paid to an employee whose principal place of employment on August 28, 2005 was in the Hurricane Katrina disaster area. Wages qualify for the credit regardless of whether the employee performs any services, or performs services at a different employer location. To qualify, the wages also must be paid between the date on which the employer's business first became inoperable due to the hurricane, and the date the business has resumed significant operations. However, the wages must be paid by January 1, 2006 in order to qualify for the credit, even if significant operations have not resumed by that date.

Employers Can Convert Unused Worker Leave into Katrina Aid

The Internal Revenue Service ("IRS") has issued guidance to employers that adopt leave-based donation programs to aid victims of Hurricane Katrina. Such programs allow employees to "donate" their accrued vacation, sick, or personal leave, and in exchange, the employer makes an equivalent cash payment to qualified tax-exempt charities providing relief to hurricane victims, provided contributions are made before January 1, 2007. These payments will not be recognized as gross income or wages for the employee and should not be included in Box 1, 3 (if applicable), or 5 of the Form W-2. Employers may either deduct these donations as a trade or business expense, or as a charitable contribution.

Employees, however, may not claim charitable contribution deductions for the value of the donated leave.

Hurricane Katrina Victims Can Use Funds from Qualified Plans

Penalty-Free Withdrawals from Retirement Plans. Normally, when an employee takes an early withdrawal from a qualified retirement plan, IRA, or IRC 403(b) annuity, the amount withdrawn is subject to a ten (10%) percent penalty for early distribution. This penalty does not apply, however, to early withdrawals of up to \$100,000 taken by those who sustained losses as a result of living in the Hurricane Katrina disaster area. Such withdrawals, known as qualified disaster-relief distributions, are includible in the withdrawing individual's gross income for tax purposes, but the tax consequences may be spread over three years. In addition, any distribution that is recontributed to a qualified plan during the three-year period beginning after the date of the disaster declaration is treated as a rollover, and therefore not subject to taxation. An amended return can be filed to claim a refund for taxes paid on distributions that are recontributed.

Extension of Deadlines for Loans from Qualified Plans. Hurricane Katrina victims who have qualified plan loan payments due between August 25, 2005 and December 31, 2006 can have those payments deferred for one year. Similarly, the period from August 25, 2005 through December 31, 2006 will be disregarded for loans to Hurricane Katrina victims in determining the maximum repayment period (generally five years) and level payment requirements.

Increased Loan Amounts Available. The amount Hurricane Katrina victims may receive as loans

from qualified plans has been increased by doubling the thresholds to the lesser of \$100,000 or 100% of the individual's account balance.

Hurricane Katrina Victims May Benefit from Extended Welfare Benefit Plan Deadlines

The period from August 29, 2005 through January 3, 2006 will be disregarded when determining certain time periods and dates for welfare benefits plan participants, beneficiaries or claimants directly affected by Hurricane Katrina. Among the time periods and dates for which the August 29, 2005 through January 3, 2006 period will be disregarded are the following:

- The 63-day break in coverage period for calculating creditable coverage;
- The 30-day period to secure creditable coverage for certain children;
- The 30-day period to request special enrollment rights in health plan;
- The 60-day period to elect COBRA continuation coverage;
- The date for making COBRA premium payments;
- The date for notifying the plan of a qualifying event;
- The date for filing a benefit claim under the plan; and
- The date for filing an appeal of a denied claim.

Extensions of Deadlines for Group Health Plans

Group health plans, their sponsors and administrators, and health insurance issuers who were directly affected by Hurricane Katrina may disregard the period from August 29, 2005 through January 3, 2006 when determining the date for providing an automatic certificate of creditable coverage and the date for providing a COBRA election notice.

Employers Can Establish Katrina Relief Foundations

Many employers have tax-exempt foundations that have created a Hurricane Katrina fund to collect donations to aid in disaster relief. Some employers are forming new tax-exempt foundations expressly for this purpose. Employers considering setting up a disaster relief fund for an existing or new tax-exempt employer foundation should keep in mind that the group of individuals who may properly receive assistance from a charitable organization must be large or indefinite enough that providing aid to them benefits the community as a whole. In addition, the tax-exempt foundation must use a reasonable and objective formula that is consistently applied to ensure that recipients are selected to receive distributions from the fund based on an objective determination of need. Under these rules, the tax-exempt foundations of large employers can usually provide assistance limited to their own employees who are affected by Hurricane Katrina. However, certain employees, such as the directors or officers of the tax-exempt foundation, may be prohibited from receiving aid from the foundation. At this time, the Internal Revenue Service is providing an expedited review and approval process for new Hurricane Katrina relief organizations seeking tax-exempt status.

CONTACT INFORMATION

We would be happy to assist you with any of the preceding matters. Please contact one of the following Brooks Pierce advisors if you would like to discuss these issues.

BROOKS, PIERCE, McLENDON, HUMPHREY & LEONARD, LLP
(336) 373-8850

Labor & Employment

William P. H. Cary
wcary@brookspierce.com

Natalie Kay Sanders
nsanders@brookspierce.com

Elizabeth V. LaFollette
elafollette@brookspierce.com

Employee Benefits

Allison M. Grimm
agrimm@brookspierce.com

Tax

William G. McNairy
wmcnairy@brookspierce.com

Mark Davidson
mdavidson@brookspierce.com

Robert W. Saunders
rsaunders@brookspierce.com

Ginger S. Shields
gshields@brookspierce.com

WWW.BROOKSPIERCE.COM

Greensboro, NC • Raleigh, NC

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