



## Tax Policy and Disaster Recovery

At times, Congress has chosen to use tax policy to provide relief and support recovery following disaster incidents. This In Focus discusses, in broad terms, disaster-related tax policy. Challenges associated with using the tax code to deliver federal financial assistance following natural disasters are also discussed.

The Internal Revenue Code contains a number of permanent disaster-related tax provisions. These include provisions providing that qualified disaster relief payments and certain insurance payments are excluded from income, and thus not subject to tax. Taxpayers are also able to deduct casualty losses and defer gain on involuntary conversions (an involuntary conversion occurs when property or money is received in payment for destroyed property). The Internal Revenue Service can also provide administrative relief to taxpayers affected by disasters by delaying filing and payment deadlines, waiving underpayment of tax penalties, and waiving the 60-day requirement for retirement plan rollovers. The availability of certain tax benefits is triggered by a federal disaster declaration. Before 2017, casualty losses were generally deductible. However, changes made in the 2017 tax revision (P.L. 115-97) restrict casualty loss deductions to federally declared disasters.

Temporary tax-related disaster relief measures were enacted following a number of major disasters that occurred between 2001 and 2017. For recent major hurricane events, temporary tax relief measures were enacted following Katrina and the other Gulf Coast hurricanes of 2005. There was not, however, a comparable package of tax benefits provided following tropical storm Irene in 2011 or Hurricane Sandy in 2012. Some general disaster provisions were available for all disasters declared in 2008 and 2009. Congress also enacted tax relief following Hurricanes Harvey, Irma, and Maria in 2017. Similar tax relief was provided following the California wildfires in 2017 and early 2018. The 2017 tax revision (P.L. 115-97) also included certain provisions that were generally applicable to 2016 or 2017 disasters.

### Tax Relief for Businesses

For businesses, hurricanes like Katrina as well as Harvey and Irma caused unprecedented property and earnings losses. Employee displacement can create labor market challenges that persist over time. Further, longer-term supply chain disruptions can make it difficult for businesses to resume operations after initial clean-up efforts are complete.

### Temporary Business Tax Relief Enacted Following Previous Disasters

In the past after certain disasters, bonus depreciation and enhanced expensing provisions have been enacted to reduce the cost of business investment in clean-up and repairs. Provisions providing accelerated cost recovery for leasehold improvements can also reduce the cost for businesses making storefront repairs in disaster zones. Other tax policy changes that have been enacted to help businesses affected by some disasters include expanded net operating loss (NOL) carrybacks (loss carrybacks allow taxpayers to offset taxable income in prior tax years), lengthened time periods for acquiring replacement property related to an involuntary conversion, and expanded rehabilitation credits for buildings damaged by disasters.

Other provisions that have been enacted following certain past disasters have attempted to support employment. These include an expanded Work Opportunity Tax Credit (WOTC) to reduce the cost of hiring employees located in the disaster area and retention credits to offset a portion of wages paid to employees by small businesses while businesses were inoperable following the disaster. Temporary tax credits for employer-provided housing have also been enacted in the past.

Other housing-related and general redevelopment provisions have been enacted following some past disasters. For real estate developers, additional low-income housing tax credits were provided for affected areas. Redevelopment following a disaster has also been supported, in some instances, by expanding new markets tax credits or by expanding authority for tax-exempt or tax credit bonds.

Other provisions might be designed to support specific industries or sectors affected by the disaster. For example, tax provisions for small timber producers and public utilities have been included in past disaster tax legislation.

### Disaster Tax Relief for Businesses: Policy Considerations

One consideration related to tax relief provisions for business is timing. The tax code is not well-suited to provide capital for clean-up, rebuilding, or recovery in the short term. Reduced tax liabilities provide a future financial benefit, but do not provide immediate access to capital that may be needed following a disaster.

For many business-related provisions, the benefit is limited to businesses with positive taxable income. Accelerated cost recovery, special deductions, and tax credits provide limited benefits to businesses with little profit or no tax liability. Further, the 2017 tax revision provided full and immediate expensing (bonus depreciation) for equipment through 2022, and increased expensing for small

businesses, limiting the scope for further accelerations of cost recovery. Businesses with limited current income or tax liability may, however, benefit from expanded NOL carrybacks.

Some critics question whether certain disaster-related tax benefits are necessary, given that much of the tax relief accrues to taxpayers who would have rebuilt without incentives. This critique raises the question of whether disaster-related tax benefits are intended to encourage certain behavior (rebuilding, for example), or with the primary purpose of providing financial relief for businesses affected by the disaster.

## Tax Relief for Individuals

Tax provisions might be used to provide financial relief to individuals who have lost property, income, or both following a disaster.

### Temporary Individual Tax Relief Enacted Following Previous Disasters

To provide relief for taxpayers experiencing a loss of property, Congress has enacted legislation following certain past disasters to expand the deduction for casualty losses (beyond what is available under the permanent provision). Following some previous disasters, Congress has also acted to expand the NOL carryback period for individual losses and to extend the time period for purchasing replacement property under an involuntary conversion.

Following some past disasters, Congress acted in other ways to change individual income tax policies to accommodate disaster-related circumstances. Specifically, in certain instances, an exclusion has been allowed for certain debt forgiven. Policies have also been enacted, in some cases, to enhance access to retirement plan funds.

To address housing issues, some past disaster tax relief packages have allowed individuals housing persons displaced by the storm an extra personal exemption and allowed individuals to exclude the value of certain employer-provided housing from income. The terms of mortgage revenue bonds have been relaxed following certain disasters, allowing certain individuals in the disaster area access to below-rate mortgages financed by these bonds.

Congress has also acted following certain past disasters to enact provisions that protect certain tax benefits. Specifically, for the earned income tax credit (EITC) and child tax credit, special provisions have allowed individuals to use previous years' earnings when calculating the credit, a policy change that could help those experiencing a loss of income following the disaster. Education-related tax credits have also been enhanced as part of certain disaster-related tax packages. Congress has also chosen, as part of disaster tax relief plans, to authorize the Secretary of the Treasury to adjust the application of tax laws to prevent the disaster from causing taxpayers to lose deductions or tax credits, or having to change their filing status.

### Disaster Tax Relief for Individuals: Policy Considerations

Many low- and moderate-income individuals have zero individual income tax liability. For these individuals, additional exclusions from income or deductions will provide little or no relief, as there is no tax burden to eliminate. Further, low- and moderate-income individuals may have limited wealth. Tax provisions designed to enhance access to certain forms of savings (e.g., retirement accounts) also provide limited relief to the least well-off.

There are also timing concerns in using the tax code to provide individuals relief following a disaster. As was noted for businesses, the tax code does not lend itself to providing immediate relief.

### Charitable Giving Incentives for Disasters

The charitable sector supports a wide range of activities associated with disaster relief and longer-term recovery. At times, Congress has acted following a disaster to provide additional tax incentives to support the charitable sector.

### Temporary Charitable Provisions Enacted Following Previous Disasters

To encourage charitable giving in the wake of a disaster, Congress has, in the past, relaxed certain income limitations associated with the deduction for charitable giving. The amount individuals can deduct for charitable use of a vehicle (the charitable mileage rate) was also temporarily increased in response to certain past disasters. Qualifying mileage reimbursements have also been allowed to be excluded from income.

Other tax incentives enacted in response to disasters have encouraged particular types of charitable giving. Provisions designed to encourage charitable contributions of food inventory and books were enacted following Hurricane Katrina. The enhanced deduction for contributions of food inventory was later made permanent, while the enhanced deduction for book inventory expired in 2011.

### Charitable Giving Incentives for Disasters: Policy Considerations

A key question regarding enhanced deductions for charitable giving is how much additional giving results from the policy change. Is it the tax benefits that drive giving, or individuals' desire to aid those affected by the storm? Another question is how much giving is for disaster-related charitable activities, as opposed to other activities or uses. Charitable giving incentives are often applied broadly, and it can be difficult to target them to a particular event or geographic region.

Another consideration is who benefits from an enhanced charitable giving deduction. On the individual side, the value of the tax benefit of the charitable deduction is highly concentrated among high-income taxpayers.

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