

Tax Filing Issues Related to the Hurricanes of 2005

- Important changes in tax law have been provided for those who were affected by Hurricanes Katrina, Rita, and Wilma last year. Check the IRS web site for information on those changes, and how they may apply to you. (hyperlink: <http://www.irs.gov/newsroom/article/0,,id=153840,00.html>) Also, for detailed information for taxpayers affected by Hurricanes Katrina, Rita, and Wilma, see IRS Publication 4492. (hyperlink: <http://www.irs.gov/pub/irs-pdf/p4492.pdf>).
- Following are some new provisions you should be aware of:
 - **CASUALTY AND THEFT LOSSES**
(hyperlink: <http://www.irs.gov/publications/p547/index.html>)
The IRS developed special rules for claiming casualty or theft losses related to property owned for personal use that was lost because of the hurricanes. Ordinarily, to figure a deduction for a casualty or theft loss of personal-use property from a particular disaster, taxpayers must reduce the loss by \$100 and also reduce their total casualty and theft losses by 10% of their adjusted gross income. For 2005, those limits are removed so that the entire amount of unreimbursed losses is deductible.
 - **CANCELLED DEBT**
(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)
Special rules exist regarding debt that has been cancelled because of the hurricane. Individuals living in the Hurricane Katrina Disaster Area on August 25, 2005, will not include in income calculation a non-business debt that is cancelled, provided that the debt is not secured by property outside the Hurricane Katrina Disaster Area.
 - **EARNED INCOME TAX CREDIT & ADDITIONAL CHILD TAX CREDIT**
(hyperlink: <http://www.irs.gov/individuals/article/0,,id=150708,00.html>)
New provisions regarding the Earned Income Tax Credit (EITC) and Additional Child Tax Credit (ACTC) exist for those affected by the hurricane. Eligible individuals from Hurricanes Katrina, Rita and Wilma may chose to calculate their EITC or ACTC using their earned income from the prior tax year, if their 2005 earned income is less than their 2004 earned income. An eligible individual is:
 - one whose taxable year included August 25, 2005, and whose main home was in the Gulf Opportunity (GO) Zone or who was displaced from the home they lived in on August 25 in the Hurricane Katrina Disaster Area; or
 - one whose taxable year included September 23, 2005, and whose main home on Sept. 23 was in the Rita GO Zone or who was displaced from the home they lived in on Sept. 23 in the Hurricane Rita disaster areas; or

- one whose taxable year included October 23, 2005, and whose main home on Oct. 23 was in the Wilma GO Zone or who was displaced from their home in the Hurricane Wilma disaster area.

The IRS recommends that you compute both your EITC and ACTC tax credits using both your 2004 and 2005 earned incomes. The IRS also recommends that you use the earned income that gives you the biggest tax benefit. If you elect to use your 2004 earned income, your election applies to both credits.

If you do not know the amount of your 2004 earned income or have lost your tax records, click <https://sa.www4.irs.gov/irfof/lang/en/irpyeiogetstatus.jsp> to retrieve that information from the IRS. Be prepared to provide the Social Security Number of the person shown first on your 2004 tax return and the date of birth for that person.

○ **EARLY DISTRIBUTIONS FROM RETIREMENT PLANS**

(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)

To qualify for tax-favored treatment, the distribution taken from an eligible retirement plan such as a qualified plan or an IRA must be made on or after Aug. 25, 2005, and before Jan. 1, 2007, to an eligible individual. An eligible individual is one whose main home was in the disaster area and who sustained an economic loss. The total amount of tax-favored distributions an individual can receive is \$100,000. An individual receiving these distributions does not have to pay the 10% additional tax on early distributions. Plus, qualified distributions are not subject to the mandatory 20% withholding.

For example, if an individual receives a qualified Hurricane Katrina distribution in 2005, that amount is includible in income, generally ratable over the year of the distribution and the following two years, but is not subject to the 10-percent additional tax on early distributions. If, in 2007, the amount of the qualified Hurricane Katrina distribution is recontributed to an eligible retirement plan, the individual may file an amended return (or returns) to claim a refund of the tax attributable to the amount of the distribution previously included in income.

○ **RETIREMENT PLAN LOANS**

(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)

For an eligible individual with an outstanding loan from a qualified employer plan on or after August 25, if the due date for any repayment on the loan occurs during the period beginning on August 25, September 23, or October 23, 2005, and ending on December 31, 2006, the due date will be delayed for one year. The allowable loan amount for eligible individuals is increased from \$50,000 to \$100,000.

- **HOPE CREDIT**
(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)
The Hope Credit for students enrolled and paying tuition at eligible educational institutions in the GO Zone for tax years beginning in 2005 or 2006 is expanded from a maximum of \$1,000 per student to 100% of the first \$2,000 in eligible expenses plus 50% of the next \$2,000 – for a maximum of \$3,000.
- **THE LIFETIME LEARNING CREDIT**
(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)
The Lifetime Learning Credit is expanded from 20% to 40%.
- **ADDITIONAL EXEMPTION FOR HOUSING DISPLACED INDIVIDUALS**
(hyperlink: <http://www.irs.gov/newsroom/article/0,,id=152734,00.html>)
The new law allows an additional exemption of \$500 in taxable years 2005 and 2006 for each Hurricane Katrina displaced individual claimed by the taxpayer.

A Hurricane Katrina displaced individual is a person (1) whose main home on Aug. 28, 2005 was in the Hurricane Katrina disaster area, (2) who is displaced from the home, and (3) who is provided housing free of charge in the taxpayer's main home for a period of 60 consecutive days which ends in the taxable year in which the exemption is claimed. A displaced individual may not be the spouse or any dependent of the taxpayer claiming the exemption. This exemption is a one-time claim and can only be claimed by one taxpayer.

Total additional exemptions cannot exceed: \$2,000 for married taxpayers filing jointly, \$1,000 for married taxpayers filing separately, and \$2,000 for all other taxpayers. To claim the additional exemption, the taxpayer must provide the taxpayer identification number of the displaced individual. The exemption is not allowed if the taxpayer receives any rent or other amount from any source in connection with the providing of housing for a displaced individual.