

HURRICANE TAX RELIEF ACTS OF 2005

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I. Overview

1. Congress worked very quickly to pass these substantial relief packages. Originally designed to cover Hurricane Katrina, the relief was extended to those areas affected by Hurricanes Rita and Wilma.
2. Total relief package is about \$6.1 billion from the Katrina Tax Relief Act and about \$8.6 million from the Gulf Opportunity Zone Act.
3. The relief isn't only for those in the disaster area. Some provisions potentially apply to all taxpayers.
4. As a general rule, the effective dates of the legislation correspond to the hurricane relief provided. Hurricane Katrina relief generally starts on August 25, 2005; Hurricane Rita relief generally starts on September 23, 2005; and Hurricane Wilma relief generally begins on October 23, 2005.

II. Definitions

I. Katrina Disaster Area

- a. An area with respect to which a major disaster has been declared by President Bush before September 14, 2005 under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act by reason of Hurricane Katrina.
- b. List of counties and parishes within the Katrina Disaster Area:
 - i. Alabama - Baldwin, Choctaw, Clarke, Greene, Hale, Mobile, Pickens, Sumter, Tuscaloosa, Washington, Bibb, Colbert, Cullman, Jefferson, Lamar, Lauderdale, Marengo, Marion, Monroe, Perry, Wilcox and Winston.
 - ii. Florida - Monroe, Broward, Miami-Dade, Bay, Collier, Escambia, Franklin, Gulf, Okaloosa, Santa Rosa and Walton.
 - iii. Louisiana - Acadia, Ascension, Assumption, Calcasieu, Cameron, East Baton Rouge, East Feliciana, Iberia, Iberville, Jefferson, Jefferson Davis, Lafayette, Lafourche, Livingston, Orleans, Pointe Coupee, Plaquemines, St. Bernard, St. Charles, St. Helena, St. James, St. John, St. Mary, St. Martin, St. Tammany, Tangipahoa, Terrebonne, Vermilion, Washington, West Baton Rouge, West Feliciana, Allen, Avoyelles, Beauregard, Bienville, Bossier, Caddo, Caldwell, Catahoula, Claiborne, Concordia, Desoto, East Carroll, Evangeline, Franklin, Grant, Jackson, LaSalle, Lincoln, Madison, Morehouse, Natchitoches, Ouachita, Rapides, Red River, Richland, Sabine, St. Landry, Tensas, Union, Vernon, Webster, West Carroll and Winn.

- iv. Mississippi - Adams, Amite, Attala, Claiborne, Choctaw, Clarke, Copiah, Covington, Franklin, Forrest, George, Greene, Hancock, Harrison, Hinds, Jackson, Jasper, Jefferson, Jefferson Davis, Jones, Kemper, Lamar, Lauderdale, Lawrence, Leake, Lincoln, Lowndes, Madison, Marion, Neshoba, Newton, Noxubee, Oktibbeha, Pearl River, Perry, Pike, Rankin, Scott, Simpson, Smith, Stone, Walthall, Warren, Wayne, Wilkinson, Winston, Yazoo, Alcorn, Benton, Bolivar, Calhoun, Carroll, Chickasaw, Clay, Coahoma, DeSoto, Grenada, Holmes, Humphreys, Issaquena, Itawamba, Lafayette, Leflore, Lee, Marshall, Monroe, Montgomery, Panola, Pontotoc, Prentiss, Quitman, Sharkey, Sunflower, Tallahatchie, Tate, Tippah, Tishomingo, Tunica, Union, Washington, Webster and Yalobusha.

2. Core Disaster Area

- a. That portion of the Hurricane Katrina disaster area determined by President Bush to warrant individual or public assistance from the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act.
- b. Counties and parishes in the core disaster area
 - i. Alabama - Baldwin, Choctaw, Clarke, Greene, Hale, Mobile, Pickens, Sumter, Tuscaloosa and Washington.
 - ii. Louisiana - Acadia, Ascension, Assumption, Calcasieu, Cameron, East Baton Rouge, East Feliciana, Iberia, Iberville, Jefferson, Jefferson Davis, Lafayette, Lafourche, Livingston, Orleans, Pointe Coupee, Plaquemines, St. Bernard, St. Charles, St. Helena, St. James, St. John, St. Mary, St. Martin, St. Tammany, Tangipahoa, Terrebonne, Vermilion, Washington, West Baton Rouge and West Feliciana.
 - iii. Mississippi - Adams, Amite, Attala, Claiborne, Choctaw, Clarke, Copiah, Covington, Franklin, Forrest, George, Greene, Hancock, Harrison, Hinds, Jackson, Jasper, Jefferson, Jefferson Davis, Jones, Kemper, Lamar, Lauderdale, Lawrence, Leake, Lincoln, Lowndes, Madison, Marion, Neshoba, Newton, Noxubee, Oktibbeha, Pearl River, Perry, Pike, Rankin, Scott, Simpson, Smith, Stone, Walthall, Warren, Wayne, Wilkinson, Winston and Yazoo.

3. Gulf Opportunity Zones (GO Zones) were created by the Hurricane Acts. Opportunity zones are defined differently from disaster areas. Opportunity zones are portions of the disaster area that are designated as in need of additional assistance.

- a. Gulf Opportunity Zone (GO Zone) – the portion of the Katrina Hurricane Disaster area determined by the president as warranting federal individual and public assistance under the Stafford Act.
- b. Rita GO Zone - the portion of the Hurricane Disaster area determined by the president as warranting federal individual and public assistance under the Stafford Act because of Hurricane Rita.



- c. Rita disaster area – an area for which the President has declared a major disaster before October 6, 2005 because of Hurricane Rita.
 - d. Wilma GO Zone - the portion of the Hurricane Disaster area determined by the president as warranting federal individual and public assistance under the Stafford Act because of Hurricane Wilma.
 - e. Wilma disaster area – an area for which the President has declared a major disaster before November 14, 2005 because of Hurricane Wilma.
4. The definitions are effective for tax years ending on or after August 28, 2005.

III. Retirement Plan Provisions

A. Retirement Plan Distributions

- 1. Up to \$100,000 of qualified distributions are exempted from the 10% penalty tax for early withdrawal.
- 2. The total distributions can't exceed \$100,000 reduced by any qualified distributions in all previous years.
- 3. A qualified distribution is any distribution from an eligible retirement plan made
 - a. On or after August 24, 2005 and before January 1, 2007 to an individual whose principal place of abode on August 28, 2005 was located in the disaster area declared for Hurricane Katrina and who suffered an economic loss due to the hurricane.
 - b. On or after September 23, 2005 and before January 1, 2007 to an individual whose principal place of abode on September 23, 2005 was located in the disaster area declared for Hurricane Rita and who suffered an economic loss due to the hurricane.
 - c. On or after October 23, 2005 and before January 1, 2007 to an individual whose principal place of abode on October 23, 2005 was located in the disaster area declared for Hurricane Wilma and who suffered an economic loss due to the hurricane.
- 4. A qualified retirement plan is
 - a. An IRA
 - b. A SIMPLE IRA
 - c. An individual retirement annuity other than an endowment contract
 - d. A qualified retirement trust



- e. A qualified annuity plan
 - f. An SEP
 - g. Eligible deferred compensation plan maintained by a governmental employer, and
 - h. An annuity contract
5. It appears that distributions from Sec. 457 plans maintained by nongovernmental authorities don't qualify for the exemption.
 6. The distributions are taxable as ordinary income.
 7. This rule doesn't apply to an excess of distributions over \$100,000.
 8. An employer plan won't be treated as violating the law simply because it treats a distribution as a qualified hurricane distribution, provided the individual doesn't receive more than \$100,000 in the aggregate from the employer's plans.
 9. In *Notice 2005-92, IRB 2005-51*, the IRS held that all Katrina distributions received during a year must be consistently treated. Presumably, this will also apply to other qualified hurricane distributions.

B. Recontribution of Retirement Plan Distributions

1. For the three-year period beginning on the day after the date of distribution, some or all of the distribution can be recontributed to an eligible retirement plan in which the distributee is a beneficiary and to which a rollover contribution can be made.
2. The aggregate amount of the repayments can't exceed the qualified hurricane distributions.
3. The payments are treated as a direct trustee to trustee rollover within the 60 day eligible rollover period.
4. Taxpayers who receive qualified hurricane distributions and pay tax on them can file an amended return and claim a refund.
5. If the distribution is from an IRA, it must be recontributed to an IRA.
6. There is no 20% withholding on qualified hurricane distributions

C. Income Averaging for Hurricane Distributions

1. A qualified hurricane distribution is included in the recipient's gross income equally over the three-year period beginning with the year the distribution was received, unless the individual elects not to apply the income averaging rules.



2. If the individual dies before the distribution has been completely reported as income, the remainder is included in the individual's income for the year of the individual's death.
3. If there is a recontribution prior to the end of the three-year period, any remaining amount to be included in income is reduced by the recontribution.

D. Home Purchase Distributions Cancelled because of Hurricane Katrina

1. Any individual receiving a qualified distribution as a first time homebuyer can repay the distribution to an eligible retirement plan by February 28, 2006 if the home purchase was cancelled due to a hurricane.
2. The distribution must have been taken after February 28, 2005 and before August 29, 2005 for home purchases or construction cancelled because of Hurricane Katrina.
3. The distribution must have been taken after February 28, 2005 and before September 24, 2005 for home purchases or construction cancelled because of Hurricane Rita.
4. The distribution must have been taken after February 28, 2005 and before October 24, 2005 for home purchases or construction cancelled because of Hurricane Wilma.
5. The contributions are treated as direct rollovers.
6. The rules apply to individuals in areas not affected by the hurricane, provided the purchase takes place in the affected area.

E. Retirement Plan Loan Repayments

1. The limits for plan loans to qualified individuals are increased for loans made after September 23, 2005 and before January 1, 2007 to the lesser of (1) \$100,000, or (2) the greater of (i) \$10,000, or (ii) the present value of the employee's nonforfeitable accrued benefit under the retirement plan.
2. A qualified individual is an individual whose principal place of abode on Aug. 28, 2005, was located in the Hurricane Katrina disaster area, and who sustained an economic loss due to Hurricane Katrina; an individual whose principal place of abode on September 23, 2005, was located in the Hurricane Rita disaster area, and who sustained an economic loss due to Hurricane Rita; or an individual whose principal place of abode on October 23, 2005, was located in the Hurricane Wilma disaster area, and who sustained an economic loss due to Hurricane Wilma.
3. An individual can only qualify for relief under one of the hurricane provisions.
4. If a qualifying individual has a retirement plan outstanding on or after one of the effective dates, the following relief provisions will be available:



- a. If the due date for any repayment occurs after the applicable effective date to December 31, 2005, the due date is delayed for one year.
- b. Any later loan repayment will be adjusted to reflect the one year delay in the due date and any interest accruing during the delay and
- c. In determining the five-year period and the term of the loan the one-year delay period is disregarded.

F. Retroactive Amendment of Retirement Plans

1. Amendments made to employee retirement plans and IRAs will be treated as operated in accordance with its terms if it is amended beginning on the legislative or regulatory amendment's effective date, and ending no later than the last day of the plan year beginning on or after Jan. 1, 2007.
2. For governmental plans, the amendment period is two years after the date that would otherwise apply.
3. To qualify for the Hurricane amendment provisions, the plan or IRA must be operated as though the amendment were in effect during the period and the amendment must apply retroactively to the period.

IV. Tax Credits for Hurricane Impact

A. Rehabilitation Tax Credit

1. The rehabilitation tax credit is increased from 20% to 26% for any certified historic structure and from 10% to 13% for qualified rehabilitated building located in the GO Zone.
2. Generally, qualified rehabilitation expenses are those made in connection with the rehabilitation of a qualified building, including renovation, restoration or construction of a building, but not a building enlargement or any new construction.
3. This provision is effective for tax years ending on or after August 28, 2005

B. Low Income Housing Credit Cap Increased

1. For 2006, 2007 and 2008 the population component of the state housing credit ceiling is increased for the GO Zone and for the states of Texas and Florida to the lesser of
 - a. The aggregate housing credit dollar amount allocated by the state housing credit agency to buildings located in the GO Zone for the calendar year or
 - b. An amount equal to \$18 multiplied by the portion of the state population located in the GO Zone using the most recent census released prior to August 28, 2005.



- c. For Texas and Florida in 2006, the credit ceilings are increased by \$3.5 million for each state.
 2. In determining the unused state housing credit ceiling, any increase in the state ceiling resulting from the changes for the GO Zone is treated as an increase in the population component of the state ceiling.
 3. A state within the GO Zone is deemed to use the credits in the following order
 - a. The additional credit cap under the GO Zone
 - b. The state's allocation of the unused state housing credit ceiling (if any) from the preceding calendar year
 - c. The current year's allocation of present-law credit
 - d. Any national pool allocations.
 4. The additional credit cap available for states within the GO Zone can't be carried forward from one year to another. This restriction does not apply for purposes of the Rita GO Zone and the Wilma GO Zone.
 5. The definition of difficult development area is changed for tax-exempt bond financed property placed in service in 2006 through 2008 in any of the GO Zones.
 6. All of these zones will be treated as difficult development zones. This means that tax-exempt bond financed property will qualify for more generous basis treatment, which will yield more generous credits.
 7. Also, this property won't be taken into account in applying the 20% population limit on difficult development areas.
 8. The low-income unit requirements for low-income housing are modified for GO Zone projects placed in service in 2006 through 2008 in nonmetropolitan areas of the GO Zone.
- C. New Markets Tax Credit
 1. An additional allocation of the new markets tax credit (\$300,000,000 for 2005 and 2006 and \$400,000,000 for 2007) is provided.
 2. The additional allocation is to be spread among qualified community development entities (CDE) for qualified low-income community investments in the GO Zone
 3. To qualify the CDE must have as a significant mission the recovery and redevelopment of the GO Zone.
 4. The carryover of any unused additional allocation is applied separately from the general allocation carryover rules.



D. Work Opportunity Tax Credit (WOTC)

1. Hurricane Katrina employees now constitute members of a targeted group for purposes of the WOTC.
2. A Katrina employee is an individual
 - a. Who had a principal place of abode in the “Hurricane Katrina core disaster area” and who is hired during the two-year period beginning on August 28, 2005 for a position the principal place of employment of which is in the “Hurricane Katrina core disaster area” or
 - b. Who had a principal place of abode in the “Hurricane Katrina core disaster area” and who is hired during the period beginning on August 28, 2005 and ending on December 31, 2005.
3. An individual providing an employer with reasonable evidence that he or she is a Hurricane Katrina employee meets the WOTC certification requirements. If that evidence later turns out to be false or incorrect, the certification is revoked and the credit for the wages is not allowed.
4. Even though the WOTC is terminated after December 31, 2005, the termination won't apply to Hurricane Katrina employees.
5. The prohibition against claiming the credit for employees who had been previously employed by the employer doesn't apply to the first hire of an employee, unless the individual was an employee on August 28, 2005.

E. Hurricane Employee Retention Credit

1. Qualified employers can claim a credit of 40% of qualified wages, up to \$6,000.
2. This credit is part of the general business credit.
3. Qualified employer
 - a. An employer conducting an active trade or business on August 28, 2005 in the GO Zone. For Hurricane Rita, an employer conducting an active trade or business on September 23, 2005 in the Rita GO Zone. For Hurricane Wilma, an employer conducting an active trade or business on October 23, 2005 in the Wilma GO Zone.
 - b. Whose trade or business is inoperable on any day after August 28, 2005 for Hurricane Katrina, after September 23, 2005 for Hurricane Rita, after October 23, 2005 for Hurricane Wilma and before January 1, 2006 because of the applicable hurricane's damage.



4. An eligible employee is one whose principal place of employment was with a qualified employer on August 28, 2005 for Hurricane Katrina, September 23, 2005 for Hurricane Rita and October 23, 2005 for Hurricane Wilma
5. Qualified wages include wages paid whether or not the employee performs any services, performs services at a different place from the principal place of employment or performs services at the principal place of employment before significant operations have resumed.
6. The qualified wage period is any day after August 28, 2005 for Hurricane Katrina, after September 23, 2005 for Hurricane Rita, after October 23, 2005 for Hurricane Wilma and before January 1, 2006 beginning on the date the business first became inoperable and ending on the date the business resumes significant operations.
7. The rules of IRC Sec. 280C apply to this credit. Thus, the wage deduction must be reduced for the credit.
8. The rules of IRC Secs. 51 and 52 apply as well. Thus, there is no credit for wages paid to dependents or relatives and members of a controlled group are treated as one employer for purposes of the credit.
9. This WOTC can't be claimed for any wages for which this credit is claimed.
10. The credit is part of the general business credit

V. Charitable Contribution Changes

A. Charitable Deduction Limitations

1. Individuals can make cash contributions to qualifying charities up to the individual's AGI, computed without regard to any NOL carryback.
2. The new limitation applies to contributions made for the period beginning on August 28, 2005 and ending on December 31, 2005.
3. For sole proprietors, S corporations and partnerships, the separate election is made at the individual owner level.
4. The deduction is allowed to the extent that the individual's contribution base (AGI without regard to any NOL carryback) exceeds the deduction for other charitable contributions.
 - a. The other charitable contributions will still be subject to the various AGI limitations (i.e. 50%, 30%, etc.).
 - b. Excess contributions can be carried over for five years, subject to the 50% charitable contribution limitation.



5. A qualifying charity is a charity described in IRC Sec. 170(b)(1)(A) other than supporting organizations described in IRC Sec. 509(a)(3).
 - a. A church or a convention or association of churches,
 - b. An organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on,
 - c. An organization the principal purpose or functions of which are the providing of medical or hospital care or medical education or medical research, if the organization is a hospital, or if the organization is a medical research organization directly engaged in the continuous active conduct of medical research in conjunction with a hospital, and during the calendar year in which the contribution is made such organization is committed to spend such contributions for such research before January 1 of the fifth calendar year which begins after the date such contribution is made,
 - d. an organization which normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under IRC 501(a) from the United States or any State or political subdivision thereof or from direct or indirect contributions from the general public, and which is organized and operated exclusively to receive, hold, invest, and administer property and to make expenditures to or for the benefit of a college or university which is an organization referred to in b. above and which is an agency or instrumentality of a State or political subdivision thereof, or which is owned or operated by a State or political subdivision thereof or by an agency or instrumentality of one or more States or political subdivisions,
 - e. A governmental unit
 - f. An organization referred to in which normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under from a governmental unit or from direct or indirect contributions from the general public,
 - g. A private foundation
 - h. an organization described in IRC Sec. 509(a)(2) or 509(a)(3). However, note the exclusion from the qualified definition of Sec. 509(a)(3) entities.
6. Individuals must elect to have the contributions treated as qualified contributions.



7. The contribution can't be for the establishment or maintenance of a segregated fund or account with respect to which the donor or someone designated by the donor has or reasonably expects to have advisory privileges with respect to distributions or investments by reason of the donor's status as a donor.
8. Qualified contributions will not be subject to the phaseout of deductions for high-income individuals, but contributions carried over to 2006 will be subject to the phaseout.
9. Corporations can also deduct qualified charitable contributions up to the amount of taxable income, provided the contributions are for relief efforts related to Hurricanes Katrina, Rita and/or Wilma.

B. Food Inventory Contributions

1. All business taxpayers (sole proprietors, S corporations and partnerships) can claim an enhanced deduction for food inventories that was only available to C corporations for inventory items donated after August 27, 2005 and before January 1, 2006.
2. For all taxpayers, the deduction is the lesser of
 - a. Basis plus one-half of the item's appreciation or
 - b. Two times the basis.
3. The donee must use the property consistent with its exempt purpose solely for the care of the ill, the needy, or infants, not transfer the property in exchange for money, other property, or services, and) provide the taxpayer a written statement that its use of the property will be consistent with these requirements. Contributed property that's subject to the Federal Food, Drug, and Cosmetic Act must satisfy its requirements on the transfer date and for 180 days before the transfer.
4. A donor must reduce the cost of sales by the lesser of the donor's basis or FMV.
5. For non-C corporations, the total deduction cannot exceed 10% of net income for the year (without regard to the food inventory deduction).
6. Only apparently wholesome food qualifies.
7. Apparently wholesome food is food intended for human consumption that meets all quality and labeling standards imposed by federal state and local laws, even though the food may not be readily marketable due to appearance, age, freshness, grade, size, surplus, or other conditions.

C. Contributions of Book Inventories

1. C corporations can also deduct an enhanced amount for qualified book contributions made after August 28, 2005 and before January 1, 2006.



2. Qualified book contributions are those made to a public school providing elementary or secondary education.
3. The school must be an educational organization that normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.
4. No deduction is allowed unless the school provides a written certification that the books are suitable for use in its educational programs and that the school will use the books in its program. "Suitable" includes currency, quantity and content.
5. There is no requirement that the contribution be used for Hurricane Katrina relief.

D. Exemption for Housing Hurricane Katrina Victims

1. For individual tax years beginning in 2005 and 2006, there is an additional \$500 exemption for each Hurricane Katrina victim for whom shelter is provided rent-free for at least 60 consecutive days.
2. The exemption can only be claimed once in 2005 and 2006 for each person, but not in both years for the same person.
3. The total exemption claimed under this provision is capped at \$2,000 (effectively 4 victims).
4. The income-based phaseouts applicable to other personal exemptions don't apply to this exemption.
5. This exemption is also allowable in computing AMT.
6. An individual qualifying for this exemption is one
 - a. Whose principal place of abode on Aug. 28, 2005 was in the Hurricane Katrina disaster area
 - b. Who is displaced from the abode and if the abode was not in the core disaster area, the abode was damaged by Hurricane Katrina or the person was evacuated from the abode because of Katrina
 - c. Who is provided housing free of charge by the taxpayer in the taxpayer's principal residence for a period of 60 consecutive days that ends in the tax year in which the exemption is claimed.
7. A taxpayers' spouse or dependent cannot be a Hurricane Katrina displaced individual with respect to the taxpayer.
8. The taxpayer claiming the exemption cannot receive any rent or other amount from any source for providing housing for a Hurricane Katrina victim.



9. In order to claim the additional exemption, the taxpayer must provide the Hurricane Katrina victim's Taxpayer Identification Number.

E. Charitable Mileage Rate for Katrina Relief

1. Any use of an auto for providing donated services to a charity for Hurricane Katrina relief from August 25, 2005 through December 31, 2006 will provide a deduction using an increased mileage rate.
2. The increased mileage rate equals 70% of the business mileage in effect on the date of the contribution, rounded to the next highest whole cent.
3. For mileage prior to September 1, 2005, the increased charitable rate will be 29¢, and for mileage from September 1, 2005 through December 31, 2005 will be 34¢. The increased mileage rate for charitable contributions in 2006 is 32¢ (.7 X 44.5¢)

F. Exclusions of Income Mileage Reimbursements

1. Reimbursements by public charities and private foundations to volunteers for using an auto to provide donated services for Hurricane Katrina relief from August 25, 2005 through December 31, 2006 aren't taxable to the extent
 - a. The amount doesn't exceed the standard mileage rate (48.5¢ from September 1, 2005 through December 31, 2005) and
 - b. The substantiation requirements for business expenses are satisfied.
2. The exclusion doesn't apply to any expenses relating to the performance of services for compensation.
3. No deduction or credit for these expenses can be claimed for these expenses.

VI. Depreciation and Other Economic Incentives for the GO Zone

A. Additional Depreciation for GO Zone Property

1. An additional 50% depreciation allowance on new qualified property placed in service is permitted.
2. The property must be placed in service on or after August 28, 2005 and before December 31, 2007. For non-residential real property and residential rental property, the property must be placed in service prior to December 31, 2008.
3. This provision is a new provision, not an extension of the original bonus depreciation provisions enacted after 9-11. However, it is very similar to that provision, so the same basic rules should apply. However, this provision permits residential rental property and nonresidential real property to qualify for the bonus depreciation deduction.



4. Qualified property must meet all of the following requirements:
 - i. It must be MACRS property with a recovery period of 20 years or less, MACRS water utility property, qualified leasehold improvements, off-the-shelf computer software, residential rental property, or nonresidential real property;
 - ii. Substantially all of the property's use must be in the active conduct of a trade or business within the GO Zone;
 - iii. The original use of the property in the GO Zone must commence with the taxpayer on or after August 28, 2005;
 - iv. The property must be purchased on or after August 28, 2005; and
 - v. There can be no written binding contract for the property's purchase in effect before August 28, 2005;
5. Under this provision, used property will qualify if the first use of the property occurs within the GO Zone (i.e. reconditioning a machine that is then used in the Zone).
6. The following property is excluded from using the 50% depreciation deduction, even if all the requirements are met:
 - a. Property for which ADS is required (note, this includes listed property if used 50% or less of the time for business);
 - b. Property used as a private or commercial golf course, a country club, a massage parlor, a hot tub facility, a suntan facility, a liquor store or a gambling or animal racing property;
 - c. Property partially or completely financed with tax-exempt bonds; or
 - d. Qualified revitalization buildings (new nonresidential real property placed in service in a renewal community) and rehab expenditures claimed as a deduction under IRC Sec. 1400I(a).
7. Self constructed property qualifies provided the construction started after August 27, 2005 and the property is placed in service prior to January 1, 2008 (January 1, 2009 in the case of residential rental and nonresidential real property).
8. The 50% bonus depreciation deduction is allowable in full for AMT, as is any depreciation deduction on qualified GO Zone property remaining after the reduction by the 50% bonus depreciation.
9. If the property is used 50% or less in a qualifying trade or business anytime during its recovery period, the deduction is recaptured.



10. A taxpayer can elect out of the bonus depreciation. The election is made on a property class by property class basis. The property class rule applies to the real property as well, so all buildings would be affected by the election.

B. Bonus Depreciation Property Placed In Service Relief

1. The Treasury Secretary is given authority to extend the January 1, 2006 placed in service date for property requiring a longer production period and noncommercial aircraft by a period not to exceed one additional year.
2. The extension must be made on a case by case basis and won't qualify unless the property will be placed in service in the GO Zone, the Rita GO Zone or the Wilma GO Zone by a taxpayer affected by one of the hurricanes or the property is manufactured in one of these zones by a taxpayer affected by a hurricane.
3. The relief can only be granted if the ability to place the property in service before January 1, 2006 was caused by a hurricane.

C. Section 179 Deduction for GO Zone Property

1. The Section 179 deduction for qualified property is increased by the lesser of \$100,000 or qualified Section 179 GO Zone property placed in service, and the investment limit is increased by the lesser of \$600,000 or the amount of qualified Section 179 GO Zone property placed in service.
2. The effective limits are \$205,000 for 2005 and \$208,000 for 2006.
3. Likewise, the limit on investment of Section 179 GO Zone property before all Section 179 deduction is lost is \$1,238,000 ($208,000 - (\$430,000 + \$600,000)$)
4. Qualified property must meet all of the following requirements:
 - i. It must be MACRS property with a recovery period of 20 years or less;
 - ii. Substantially all of the property's use must be in the active conduct of a trade or business within the GO Zone;
 - iii. The original use of the property in the GO Zone must commence with the taxpayer on or after August 28, 2005;
 - iv. The property must be purchased on or after August 28, 2005; and
 - v. There can be no written binding contract for the property's purchase in effect before August 28, 2005;
5. If the taxpayer first uses the property in the GO Zone, then used property may qualify for the increased deduction. If, however, the property was used by another taxpayer within the GO Zone, only the normal Section 179 limits apply.



6. The following property is excluded from using the 50% depreciation deduction, even if all the requirements are met:
 - a. Property for which ADS is required (note, this includes listed property if used 50% or less of the time for business);
 - b. Property used as a private or commercial golf course, a country club, a massage parlor, a hot tub facility, a suntan facility, a liquor store or a gambling or animal racing property; or
 - c. Property partially or completely financed with tax-exempt bonds.
7. Self constructed property qualifies provided the construction started after August 27, 2005 and the property is placed in service prior to January 1, 2008 (January 1, 2009 in the case of residential rental and nonresidential real property).
8. The property must be acquired on or after August 28, 2005 and placed in service prior to January 1, 2008.

D. Demolition and Cleanup Costs

1. 50% of the expenditures for demolition and cleanup that would ordinarily be capitalized may be expensed if incurred or paid on or after August 28, 2005 and before January 1, 2008 in a GO Zone.
2. Qualified costs are those paid or incurred for removal of debris or the demolition of real property located in the GO Zone if the real property is
 - a. Used in a trade or business or for the production of income or
 - b. Is inventory for the taxpayer.

E. Environmental Remediation Costs

1. Qualified environmental remediation expenses paid or incurred with a qualified contaminated site located in the GO Zone may be deducted through December 31, 2007.
2. Expenses for cleaning up petroleum products in the GO Zone can also qualify for the deduction through December 31, 2007.
3. This provision is effective for tax years ending after August 28, 2005.

F. Reforestation Expenses

1. The maximum expensing limitation for reforestation expenses paid or incurred in any of the hurricane GO Zones is increased to the lesser of
 - a. \$10,000 (\$5,000 if married filing separately) or



- b. The amount of reforestation expenses incurred or paid during the tax year for qualified timber property located in these zones.
 - 2. The increased deduction is not available to taxpayers that hold more than 500 acres of qualified timber property, REITs and publicly traded corporations.
 - 3. Lessors may claim the expense deduction, unless the lessor leases more than 500 acres of timber.
 - 4. If the property is located in the GO Zone, the increased deduction applies to expenditures paid or incurred on or after August 28, 2005 and before January 1, 2008. If the property is located in the Rita GO Zone, the increase applies to expenditures paid or incurred on or after September 23, 2005 and before January 1, 2008. If the property is located in the Wilma GO Zone, expenditures paid or incurred on or after October 23, 2005 and before January 1, 2008.
 - 5. This provision is effective for tax years ending on or after August 28, 2005.
- G. NOL Carryback for GO Zone Recovery Losses
- 1. For tax years ending on or after August 28, 2005, there is a five-year carryback for GO Zone NOLs.
 - 2. GO Zone casualty losses are any uncompensated loss from a sale, exchange or conversion of property located in the GO Zone, allowable as a deduction under IRC Sec. 165 and resulting from Hurricane Katrina.
 - a. A GO Zone casualty loss included in the NOL can't be treated as occurring in a prior tax year.
 - b. The loss must be reduced by any gain recognized from an involuntary conversion of property in the GO Zone resulting from Hurricane Katrina.
 - 3. A GO Zone loss includes moving expenses paid or incurred after August 27, 2005 and before January 1, 2008 by taxpayers whose principal place of abode was in the GO Zone before August 28, 2005, who could not remain there because of Hurricane Katrina and whose principal place of employment after the moving expense is located in the GO Zone.
 - a. The former and new residence can be the same residence if it was initially vacated due to Hurricane Katrina.
 - b. Taxpayers who pay the moving expenses of a prospective employee and later employ the individual in the GO Zone can include the expenses in the NOL.
 - 4. A GO Zone loss includes any expense paid to temporarily house employees whose principal place of employment is in the GO Zone paid or incurred on or after August 28, 2005 and before January 1, 2008.



5. A GO Zone loss includes depreciation deductions of GO Zone property, which includes nonresidential real property and residential rental property.
 - a. Substantially all of the use of the property must be in the GO Zone
 - b. The property must have been used in an active trade or business by the taxpayer in the GO Zone.
 - c. The original use of the property must have commenced on or after August 28, 2005.
 - d. The property must be purchased on or after August 28, 2005, with no prior binding agreement in place.
 - e. The property must be placed in service on or before December 31, 2007 or December 31, 2008 in the case of nonresidential real property and residential rental property.
 - f. Property using ADS depreciation, tax-exempt bond financed property and qualified revitalization buildings for which the taxpayer has elected the deduction don't qualify.
 - g. Property used as a private or commercial golf course, a country club, a massage parlor, a hot tub facility, a suntan facility, a liquor store or a gambling or animal racing property doesn't qualify.
6. A GO Zone loss includes any deduction for repair expenses incurred after August 27, 2005 and before January 1, 2008 attributable to damage connected with Hurricane Katrina on or for property located in the GO Zone.
7. The NOLs arising from GO Zone losses are applied separately, after other NOLs are taken into account.
8. GO Zone NOLs are subject to the 90% AMTNOL limitation.
9. A taxpayer can elect out of the carryback. The election must be made by the due date of the tax return, including extensions for the year of the NOL. Once made, the election is irrevocable for that year.
10. This provision applies to losses arising in tax years ending on or after August 28, 2005.

H. Public Utility Losses

1. A public utility located in the GO Zone can elect to treat a casualty loss as a specified liability loss if the loss would be allowed under IRC Sec. 165, the loss arose because of Hurricane Katrina and the taxpayer elects the treatment.



2. The public utility casualty loss is offset by any gains recognized from involuntary conversions of utility property as a result of Hurricane Katrina.
 3. The election is to be made in a manner prescribed by the IRS by the due date, including extensions for filing the taxpayer's return during the year of loss.
 4. A loss on public utility property in the GO Zone can be deducted in the fifth tax year preceding the year of the disaster.
 5. Public utility property for these provisions is property used predominantly in furnishing or selling
 - a. Electrical energy, water, or sewage disposal services
 - b. Gas or steam through a local distribution system
 - c. Telephone or other communication services if furnished or sold by the Communication Satellite Corporation for purposes authorized by the Communications Satellite Act of 1962
 - d. Transportation of gas or steam by pipeline
 6. For purposes of the specified liability loss election, the property is public utility property only if the rates for the services are set by a regulator.
 7. The statute of limitations for a claim filed will not expire earlier than one year after December 21, 2005.
 8. The provision applies to tax years ending on or after August 28, 2005.
- I. Five Year NOL Carryback for Certain Timber Losses
1. NOLs attributable to qualified timber property in one of the GO Zones can be taken into account in determining the amount of a farming loss that is eligible for a five-year carryback under the NOL rules.
 2. This provision is not applicable to
 - a. Publicly traded companies or REITS
 - b. Taxpayers who hold more than 500 acres of qualified timber property taking into account property held inside and outside hurricane zones on the applicable date.
 3. Qualified timber is at least one acre of a woodlot or other site located in the United States which will contain trees in significant commercial quantities and which is held by the taxpayer for the planting, cultivating, caring for, and cutting of trees for sale or use in the commercial production of timber products.



4. The losses only apply to the losses attributable to the portion of the tax year that begins on or after the applicable date for the GO Zone and before January 1, 2007.
5. This provision applies to losses arising in tax years ending on or after August 28, 2005.

VII. Other Tax Relief Provisions

A. Deductions and Income

I. Limitations on casualty losses

- a. The \$100 floor and the 10% of AGI floor doesn't apply to an losses arising in Hurricane Katrina disaster area on or after August 25, 2005, in the Hurricane Rita disaster area on or after September 23, 2005 or in the Hurricane Wilma on or after October 23, 2005.
- b. Casualty and theft losses are treated as a separate deduction from other casualty losses.
- c. The new rules appear to apply in 2005 or, if the special disaster loss election is made, in 2004.

2. Discharge of Debt Related to Katrina

- a. Any cancellation of a nonbusiness debt that would otherwise be taxable is excluded from income if the taxpayer's principal place of abode on August 25, 2005 was in the core disaster area or in the Hurricane Katrina disaster area and the individual suffered an economic loss because of Katrina on or after August 25, 2005 and before January 1, 2007.
- b. No exclusion applies to business debts or to an debt to the extent that real property securing the debt is located outside the Hurricane Katrina disaster area.
- c. The exclusion applies to "applicable entities" which are generally the following entities:
 - i. an executive, judicial, or legislative agency
 - ii. any financial institution
 - iii. any credit union
 - iv. any corporation that is a direct or indirect subsidiary of an entity described in i. or ii. which, by virtue of being affiliated with that entity, is subject to supervision and examination by a Federal or State agency regulating those entities



- v. the Federal Deposit Insurance Corporation (FDIC), the Resolution Trust Corporation, the National Credit Union Administration, certain other Federal executive agencies, and any successor or subunit of any of them
 - vi. any other organization a significant trade or business of which is the lending of money.
- d. Any income exclusion must reduce the taxpayer's attributes as provided in IRC Sec. 108.

3. Replacement period for Katrina-Related Involuntary Conversions

- a. The replacement period for property that is involuntarily converted due to Hurricane Katrina is extended from three years to five years.
- b. Requirements for applying the five-year replacement period.
 - i. the converted property is located in a Hurricane Katrina disaster area
 - ii. the property was involuntarily converted after August 24, 2005 because of Hurricane Katrina
 - iii. substantially all of the use of the replacement property is within the Hurricane Katrina disaster area.

B. Credits and Incentives

I. Earned Income Tax Credit (EITC)

- a. The EITC and refundable child credit for the tax year including August 25, 2005 for Katrina victims, September 23, 2005 for Rita victims and October 23, 2005 for Wilma victims can be computed using the earned income from the prior year if the 2005 earned income is less than that of the prior year. This election to use the prior year must apply to both the EITC and the refundable credit.
- b. Individuals who can use this provision are those whose principal place of abode was in the core disaster area or in the Hurricane Katrina disaster area, the Hurricane Rita disaster area or the Hurricane Wilma disaster area and the individual was displaced from his or her principal place of abode because of one of the hurricanes.
- c. If there is a joint return for the tax year including the applicable date, the election applies if either spouse is a qualified individual. The earned income for the prior year is the sum of each spouse's earned income in the prior year.
- d. The election to use the prior year is disregarded for purposes of computing gross income in the election year or any other Internal Revenue Code provision.



- e. An incorrect use of earned income because of this election is treated as a mathematical or clerical error.
2. IRS Authority to Adjust the Internal Revenue Code
- a. The IRS is given authority to make adjustments to the application of the Internal Revenue Code and federal tax laws in 2005 and 2006, as appropriate to ensure that taxpayers do not lose any deduction or credit, or experience a change of filing status due to temporary relocations because of Hurricanes Katrina, Rita or Wilma.
 - b. Any adjustments must ensure that an adjustment is not taken into account by more than one taxpayer for the same tax benefit.
3. Suspension of Employment and Excise Taxes
- a. Employment taxes and excise taxes are added to the list of items that may be suspended for up to one year as the result of a presidentially declared disaster.
 - b. The effective date is any period the time for which performing an act has not expired before August 25, 2005.
 - c. Congress extended legislatively the filing and payment relief period to taxpayers affected by Hurricane Katrina to February 28, 2006.
4. Housing Relief for Individuals Affected by Hurricane Katrina
- a. A qualified employee's income doesn't include the value of in-kind lodging provided by a qualified employer to the employee, his/her spouse or family for any month during the six month period beginning on January 1, 2006.
 - b. A qualified employee is one who, on August 28, 2005 had a principal residence in the GO Zone and who performs substantially all of his/her services in the GO Zone for a qualified employer that furnishes the lodging.
 - c. A qualified employer is any employer with a trade or business located in the GO Zone.
 - d. The exclusion cannot exceed \$600 for any month for which the lodging is provided.
 - e. An employer is also entitled to a credit for providing lodging to Hurricane Katrina victims.
 - i. The credit is 30% of the value of lodging furnished in-kind to a qualified employee.
 - ii. The credit can't exceed \$180 ($\$600 \times .3$) per month for each qualified employee.



- iii. The credit period begins on January 1, 2006 and ends on July 1, 2006
- iv. The credit is part of the general business credit.
- v. An employer cannot take a deduction for the credit.

5. Hope and Lifetime Learning Credits

- a. For students enrolled in an eligible institution in the GO Zone, the Hope Credit is increased to 100% of the first \$2,000 of qualified tuition and related expenses and 50% of the next \$2,000 of qualified expenses for a maximum credit of \$3,000 per eligible student.
- b. The Lifetime Learning Credit rate is doubled to 40%.
- c. Qualified expenses for this purpose includes those defined under IRC Sec. 529 qualified tuition programs, which includes room and board for students attending at least half-time.

6. Tax Exempt Bonds for Rebuilding GO Zone

- a. GO Zone tax-exempt private activity bonds can be authorized for issue anytime after 2005 and prior to 2011 to finance construction and repair to real estate and infrastructure in the GO Zone.
- b. The GO Zone bonds are in addition to other qualified private activity bonds authorized under the state's volume cap.
- c. Qualified GO Zone bonds are treated as qualified mortgage bonds or as exempt facility bonds.
- d. GO Zone bonds can be issued by Alabama, Mississippi, Louisiana or any political subdivision thereof.
- e. GO Zone bonds must meet state law bond issue requirements. Thus, if approval by the state bond commission is required, the approval must be obtained. If there is no state bond commission, the governor must designate the bond issue.
- f. Proceeds can't be used to finance property used as a private or commercial golf course, a country club, a massage parlor, a hot tub facility, a suntan facility, a liquor store or a gambling or animal racing property.
- g. GO Zone bonds can be treated as exempt facility bonds or qualified mortgage bonds.
- h. Qualified mortgage bonds are generally available only for first time homebuyers for the purchase of an owner-occupied, single family residence, with an



exception for residences in targeted areas. The GO Zone is treated as such a targeted area.

- i. The limit for qualified home improvement loans for financing alterations, repairs and improvements to an existing residence is usually limited to \$15,000. The GO Zone limit is \$150,000.
- j. All mortgages must be made to individuals with family income of 140% or less of the applicable median family income.
- k. The applicable family income is the greater of the area median gross income for the area in which the residence is located or the statewide median gross income for the state in which the residence is located.
- l. GO Zone bonds are exempt facility bonds if 95% or more of the net proceeds are used for the following projects:
 - i. Any qualified residential project in the GO Zone
 - ii. Acquisition, construction, reconstruction and renovation of nonresidential real property in the GO Zone
 - iii. Acquisition, construction, reconstruction and renovation of public utility property in the GO Zone
- m. Qualified residential projects are those in which 20% or more of the units are occupied by individuals with incomes of less than 60% or less of the area median gross income or 40% of the units are occupied by individuals with incomes of less than 70% of the area median gross income.
- n. The total face amount of qualified GO Zone bonds that can be issued can't exceed \$2,500 multiplied by the percentage of the state's population in the GO Zone, based on pre-August 28, 2005 census data.
- o. GO Zone bonds aren't subject to the annual limits on private activity bonds that can be issued by a state.
- p. For property acquired with GO Zone bonds, rehab expenses must equal or exceed 50% of the building cost.
- q. Excess earnings on arbitrage (the difference between the earnings and what the earnings would have been if the funds had been invested at the same interest rate as the bonds) are exempted from the requirement to be paid to the government for 24 months for GO Zone bonds that are treated as exempt facility bonds.
- r. GO Zone bond interest is not an AMT preference item.



- s. Repayments of loans financed with GO Zone bonds may not be used to make additional loans.
7. Income Certification Requirements for Qualified Residential Property
- a. Certification requirements to determine eligibility for tenants are relaxed for those displaced by Hurricane Katrina.
 - b. Owners of qualified rental projects can rely on the representations of prospective tenants displaced by Hurricane Katrina in determining whether they meet the income eligibility test.
 - c. To qualify, the tenancy must begin within the six month period beginning on the date of displacement as a result of Hurricane Katrina.
8. Mortgage Revenue Bond Restrictions
- a. The mortgage revenue bond restrictions are modified through 2010 for residences located in any of the GO Zones.
 - b. The first time homebuyer requirement is waived and the purchase price and family income limitations are relaxed.
 - c. The acquisition cost of each residence financed under the same issue can't exceed 110% of the average area purchase price. The average purchase price is the average area purchase price of a single-family residence for residences purchased within the most recent 12-month period for which sufficient statistical information is available.
 - d. The family income requirement is satisfied in the Rita and Wilma GO Zones if the financing provided under the issue is for mortgagors whose family income equals or is less than 140% of the applicable median family income.
9. Advance Refunding for Tax-Exempt Bond Issuers in Gulf Coast States
- a. Qualified Sec. 501(c)(3) bonds and certain governmental bonds issued by Alabama, Louisiana or Mississippi or any of their political subdivisions are allowed one advance refunding in addition to the advance refunding otherwise allowable.
 - b. Qualified bonds can issue refunding bonds more than 90 days before the original bond is to be redeemed, including exempt facility bonds for airports, docks or wharves.
 - c. Qualified Bonds are those outstanding on August 28, 2005 and the refunding is allowed after December 21, 2005 and before January 1, 2011, and are limited to issues for which all other permissible advance refundings were exhausted by August 28, 2005.
 - d. The governor must designate the advance refunding bond for these purposes.



- e. The maximum amount of the bond issue is \$4.5 billion for Louisiana, \$2.25 billion for Mississippi and \$1.125 billion for Alabama.

10. Gulf Tax Credit Bonds

- a. Alabama, Mississippi and Louisiana are authorized to issue a total of \$350 million in Gulf tax credit bonds in 2006.
- b. There is also an individual state limit – Louisiana - \$200 million; Mississippi \$100 million and Alabama \$50 million.
- c. A bond is qualified if it meets the following requirements:
 - i. The bond is issued Alabama, Louisiana or Mississippi;
 - ii. 95% percent or more of the bond proceeds are used to pay off qualified bonds issued by a state or other governmental unit, or to loan to political subdivisions that will use the funds to pay off its own qualified bonds;
 - iii. The governor of the issuing state designates the bond as a Gulf tax credit bond;
 - iv. The bond is a general obligation bond, issued in registered form
 - v. The bond's maturity doesn't exceed two years;
 - vi. The bond is issued in 2006; and
 - vii. The state matching requirement is satisfied with respect to the bond. The state must pledge to match the bond amount with other funds to be used for the same payoffs and loans and such payments are made equally from the bonds and pledged funds.
- d. The bonds can be used to extend the maturity of existing obligations by two years at lower interest rates, but 95% or more of the proceeds must be used to pay off state or local obligations outstanding on August 28, 2005.
- e. Exceptions to the qualified bond rule are:
 - i. Private activity bonds
 - ii. A bond for which a refunded or refunding bond is outstanding
 - iii. Any bond issue used (wholly or partially) to finance any prohibited facility (i.e. golf course, country club, etc.)



- f. Bond holders are allowed a credit equal to the interest the bond would otherwise pay, calculated by multiplying the face amount of the bond by a credit rate to be determined by the IRS.
- g. Credit dates are 3-15, 6-15, 9-15 and 12-15, with prorations for quarters where the bond is redeemed or matures.
- h. The credit is refundable and if coming through a pass-through entity can't exceed the owner's tax on the entity income.
- i. The bond issuers must meet the arbitrage rules and must file information returns with the IRS like those required for tax-exempt bonds.

11. Designation of Savings Bonds as Gulf Coast Recovery Bonds

- a. Congress has suggested the Secretary of Treasury designate one or more U.S. Savings Bond series as Gulf Coast Recovery Bonds
- b. No special treatment is to be accorded such bonds.

12. Tax Deadline Postponement

- a. Deadlines for service personnel in combat zones that can be postponed includes both employment and excise taxes.
- b. The earliest date for tax deadlines for filings affected by Hurricane Katrina, Rita or Wilma is February 28, 2006.

VIII. Technical Corrections

A. The Hurricane Relief Acts contained many technical corrections as part of the overall bill.

- 1. For tax years beginning after 12-31-05, a taxpayer may elect to treat all combat pay that is otherwise excludable from income as earned income for purposes of the earned income credit.
- 2. Suspension of Interest and Penalties
 - a. The suspension of interest rules don't apply to listed transactions and undisclosed reportable transactions for interest accruing on or before 10-3-04.
 - b. However, taxpayers participating in the IRS settlement initiative announced in *Announcement 2005-80, IRB 2005-46, 967* will remain eligible for the interest abatement.
- 3. The IRS' authority to use proceeds from undercover operations to pay additional expenses for conducting the operation is extended through 12-31-06.



4. IRS' authority to disclose taxpayer identity information and signatures to any state agency, body or commission in order to carry out a combined fed/state employment tax reporting program is extended through 12-31-06.
5. IRS' authority to disclose returns and return information to investigate terrorist incidents, threats or activities or intelligence analyzing such activities is extended through 12-31-06. Disclosure can also be made to the Justice Department for use in obtaining an *ex parte* application to a federal judge or magistrate for an order to open the return to federal law enforcement or intelligence officers personally and directly involved in investigating, responding to or analyzing intelligence of any terrorist incident, threat or activity.
6. IRS' authority to disclose certain return information to the Department of Education to establish a repayment amount for a student loan under an income-contingent repayment program is extended through 12-31-06.
7. The five-year required holding period for personal residences acquired in a like-kind exchange is extended to any person whose basis in the principal residence is determined in whole or in part by reference to the basis in the taxpayer's hands (i.e. gift, divorce, etc.) after 10-22-04.
8. For tax years beginning after 12-31-03, the state and local sales tax deduction is not applicable for AMT.
9. A custodial parent transfers the right to claim the dependency exemption to the noncustodial parent by a written declaration that must be attached to the noncustodial parent's tax return.
 - a. The right to claim the exemption need not be set forth in the divorce or separation agreement
 - b. A noncustodial parent can claim the exemption if:
 - i. The child receives over one-half his or her support from the parents during the year
 - ii. The parents are divorced or legally separated under a separate maintenance decree or written separation agreement or have lived apart at all times during the last six months of the calendar year
 - iii. One or both parents had custody for more than one-half the calendar year
 - iv. Form 8332 is signed by the custodial parent
 - v. Form 8332 is attached to the noncustodial parent's return (Form 8332 must be attached for each year, even if the custodial spouse waives the exemption permanently)
 - c. This provision is effective for tax years beginning after 12-31-04.



10. Effective for tax years beginning after 12-31-04, a taxpayer can claim the Dependent Care Credit for expenses incurred for an individual who is physically or mentally incapable of self care who lives with the taxpayer for more than six months, if the individual can be claimed as a dependent by the taxpayer. Individuals for whom an exemption could be claimed except for the fact that the person had income exceeding the exemption amount, filed a joint return or was claimed on another's tax return also qualify.
11. Effective for tax years beginning after 12-31-04, a Health Savings Account (HSA) can be used to pay the medical costs of a dependent or a person for whom an exemption could be claimed except for the fact that the person had income exceeding the exemption amount, filed a joint return or was claimed on another's tax return.
12. Domestic Production Deduction Corrections
 - a. The W-2 wage limitation is 50% of the W-2 wages of the taxpayer reported on a return filed with the Social Security Administration no later than 60 days after its extended due date.
 - b. Qualified production activities income is not reduced by the the domestic production deduction.
 - c. Construction, engineering and architectural activities must relate to real property and constitute the active conduct of a trade or business.
 - d. Proceeds from leasing, renting, licensing, selling, exchanging or otherwise disposing of land doesn't constitute domestic production gross receipts.
 - e. Contracts with the federal government qualify for the deduction if the Federal Acquisition Regulation requires that title or risk of loss be transferred to the federal government before the process is complete.
 - f. The definition of an expanded affiliated group (EAG) is clarified to provide that a corporation must own more than 50% of a sub's stock in order to claim the deduction for the sub's income.
 - g. If all the capital and profits interests of a partnership are owned by the same EAG at all times during the year, then the partnership and all members of the group are treated as a single taxpayer.
 - h. Several clarifications were made for partnerships and S corporations
 - i. The deduction is determined at the partner or shareholder level
 - ii. In computing the deduction, each partner takes into account its share of the items necessary to calculate the Sec. 199 deduction, not its share of the entity's Sec. 199 deduction



- iii. A pass-through owner's share of W-2 wages is the lesser of its allocable share of the entity's W-2 wages or twice the applicable percentage of qualified production activities income attributable to its receipts, less allocable expenses.
 - iv. Trusts and estates will allocate the various items to compute the Sec. 199 deduction as prescribed in regulations issued by the IRS.
 - v. Items arising in a tax year of a pass-through entity beginning before 1-1-05 are not taken into account for purposes of the deduction at the owner level.
 - vi. An agricultural or horticultural coop patron can claim a Sec. 199 deduction if the patron receives a patronage dividend or per-unit retain allocation attributable to Sec. 199 activities and the coop elects to pass that deduction through.
 - vii. The AMT Sec. 199 deduction is generally the same as for regular tax. However, if a corporation's AMTI is less than the applicable percentage of qualified production activity income (QPAI), the deduction will be less. For AMT purposes, QPAI will be calculated without regard to adjustments made under IRC Secs. 56, 57, 58 and 59.
 - viii. The Sec. 199 deduction is not taken into account in determining a regular tax or AMT NOL or the amount of any NOL carryback or carryover.
 - ix. In computing the Sec. 199 deductions, exempt organizations must use UBTI and AMTI, not taxable income.
 - x. The IRS is given specific authority to issue regulations to prevent more than one taxpayer from claiming a Sec. 199 deduction with respect to the same economic activity.
 - xi. These provisions are effective for years beginning after 12-31-04.
13. Electric utility companies can elect to carryback a specified amount of an NOL from 2003, 2004 and 2005 to each of the five tax years preceding the year of loss
 14. For purposes of making the election to expense certain film and TV productions (the election begins after 2008), each episode of a TV series is treated as a separate production.
 15. The provisions relating to railroad track maintenance are modified to clarify that each mile of track can be taken into account only once for purpose of the track maintenance credit, the assignment of a mile of track by a Class II or Class III railroad can be made once a year
 16. Commercial aircraft as well as any property with a longer production period separately qualify for the extended January 1, 2006 service date under the bonus depreciation rules.



17. A shipbuilder under a qualified naval shipbuilding contract can use the percentage of completion/capitalized cost method for the first five years of the contract starting with the construction commencement year. Further, the adjustments required under IRC Sec. 481 don't apply to accounting method changes under this section.
18. The organizational expense amortization rules are clarified to provide that the partnership rather than a partner is the taxpayer that can deduct the organizational expenses.
19. For treating entertainment expenses as compensation, the term "specified individual" is modified to include any person to whom the taxpayer has provided entertainment that is attributable to a specified individual.
20. Property with a long production period and noncommercial aircraft are eligible for the 50-percent bonus depreciation rate if the property or noncommercial aircraft is acquired pursuant to a binding written contract that was entered into after May 5, 2003, and before January 1, 2005. This property must be placed in service before January 1, 2006.
21. The cross references for New York Liberty Zone bonus depreciation are clarified.
22. For MACRS depreciation, the term "solar energy" property is any equipment that uses solar or wind energy.
23. Several provisions dealing with the 100 shareholder limit for S corporations were amended.
 - a. The election requirement for treating all family members as one shareholder has been repealed.
 - b. The date for determining whether a common ancestor is more than six generations removed from the youngest generation is the latest of the date the S election is made, the earliest date that a family member first holds stock in the corporation or 10-22-04.
 - c. The estate of a family member is not treated as a family member for purposes of determining the number of shareholders.
 - d. The definition of adopted individuals and foster children is amended to conform to the new, uniform definition of a "child".
24. The effective date for transfers of suspended losses to a spouse or incident to a divorce applies to transfers after 12-31-04
25. IRC Sec. 734 is amended to clarify that the mandatory basis adjustments must be made when there is a distribution of property to a partner with respect to which there is a substantial basis reduction (more than \$250,000) whether or not there is an IRC Sec. 754 election in place.



26. Bank holding companies or depository institution holding companies can elect S corporation status even if IRAs or Roth IRAs own stock in the bank or depository institution.
27. For S corporations, the exclusion of interest and dividend income from the passive income rules is extended to savings and loan holding companies.
28. Qualified Sub S subsidiaries are treated as separate entities for purposes of information return reporting.
29. The conversion of a corporation to S corporate status results in a LIFO recapture. The increase in corporate tax as a result of the LIFO recapture isn't subject to the rules that prohibit adjustments of the corporation's earnings and profits, and reduce a shareholder's basis in the stock by corporate expenses that are not deductible or chargeable to a capital account.
30. The parent's basis in built-in loss property that is distributed in a tax-free subsidiary liquidation is limited to the property's FMV. In an IRC Sec. 351 transfer of built-in loss property, the election of the parties is now to be made in a manner and form prescribed by the IRS.
31. The law clarifies that a corporate transferor in a D reorganization recognizes gain upon the distribution property, including cash, to its creditors to the extent the amount of cash plus the fair market value of the property distributed exceeds the basis of the transferred assets, less any liabilities assumed by the subsidiary.
32. In order for the stock not to be limited and preferred as to dividends, the chance that dividends exceeding any limitation or preference must be real and meaningful.
33. Open-loop biomass produced electricity can qualify for the renewable electricity production credit.
34. It is no longer necessary for solid refined coal be synthetic to claim the credit for qualified energy resources.
35. Estimated tax payments will not include the receipt of a credit for owning a clean renewable energy bond.
36. The phase-out of the credit for production from advanced nuclear power facilities is clarified to provide that the phase-out of the credit is indexed for inflation, but the credit rate is not.
37. Air pollution control facilities used with a coal-fired electrical generation plant placed in service before 1-1-76 qualify for the 60- month amortization.
38. No election is required to claim the credit for producing fuel from unconventional sources.



39. IRC Sec. 1250 is amended to eliminate the reference to the deduction for energy-efficient commercial buildings thus subjecting the deduction to recapture under IRC Sec. 1245.
40. The annual dollar limitations for the residential alternative energy credit are applied without regard to any carryover of the credit from a prior year.
41. The alternative motor vehicle credit on a vehicle sold to a tax-exempt entity becomes part of the general business credit.
42. Credits for installing alternative fueling stations for property sold to a tax-exempt entity are limited to the business tax credit of up to \$30,000, not the \$1,000 limit applicable to noncommercial taxpayers.
43. Energy research expenses for research conducted outside the US, Puerto Rico or any US possession aren't taken into account in determining the 20% of amounts paid or incurred to an energy research consortium.
44. The foreign tax need not be recomputed for purposes of computing the AMT for a farmer or fisherman who elects to use income averaging.
45. Estates are now treated equally with other entities and can expense up to \$10,000 of reforestation expenses. Trusts may elect to amortize their reforestation expenditures over 84 months.
46. Special rules for determining basis and gains or losses pursuant to exchanges or distributions ordered by the SEC for public utility holding companies are repealed.
47. The law is clarified to provide that, for assessing penalties on a failure to disclose a reportable or listed tax shelter transaction, the penalty applies to returns and statements due after 10-22-04, without regard to the original or extended due date for the return or statement.
48. The various penalty provisions for failing to report tax shelter transactions and other tax avoidance transactions are coordinated.
 - a. Underpayments from a listed or reportable transaction are not subject to the IRC Sec. 6662 penalties if a IRC Sec. 6662A penalty is assessed.
 - b. IRC Sec. 6662A does not apply to underpayments to which an IRC Sec. 6663 (fraud) penalty.
 - c. The reasonable cause exception for the IRC Sec. 6662A penalty doesn't apply to tax advisor opinions that were issued, relate to transactions or relate to returns filed before 10-22-04.
 - d. The IRC Sec. 6662A penalty doesn't apply to an understatement for which an IRC Sec. 6662 penalty is imposed if the gross valuation misstatement provision is applied.



49. For purposes of the extended statute of limitations applicable to undisclosed reportable transactions, a material advisor as defined in Reg. 301.6112-1(c)(2) applies to advice rendered before 10-22-04.
50. Those organizers and sellers of tax shelter interests required to maintain lists of persons who purchased tax shelters prior to 10-22-04 must continue to retain those lists and must provide that information to the IRS upon written request.
51. For tax-exempt use property treated as such other than because it was leased to a tax-exempt entity, the deduction limitation rules under IRC Sec. 470 are effective for property acquired after 3-12-04.
52. There are a number of technical corrections affecting nonqualified deferred compensation plans.
 - a. The restrictions on the use of certain funding methods for nonqualified deferred compensation arrangements apply to all deferred compensation as of 1-1-05, not merely to compensation deferred on or after that date.
 - b. The additional tax and interest imposed is not part of the regular tax for AMT or refundable tax credit purposes.
 - c. An election deferring scheduled distributions from nonqualified arrangements must defer all of the payments to which it applies by at least five years.
53. Roth contributions for prior years reduce the \$15,000 cap for catch-up contributions to a 403(b) plans by 15 year employees of educational, health care and religious organization.
54. The special rule allowing up to \$3,000 in annual 403(b) contributions on behalf of foreign missionaries, even if their compensation is less than that amount is restored.
55. A REIT can cure *diminimis* failures of the asset tests, other than the 5% and 10% tests, by the same procedures used to correct larger failures of the same tests.
56. Securities of a partnership held by a REIT prior to 10-22-04 that would have qualified as straight debt securities if the 2004 Jobs Act had never been enacted will continue to qualify while held by the REIT (or its successor) until the earlier of the disposition or the original maturity date of such securities.
57. For REMICS, only obligations originated by a government entity will be treated as principally secured by an interest in real property under the definition of a qualified mortgage.
58. Taxpayers can identify straddles as identified straddles with a clear and unambiguous identification in their books and records without regard to whether guidance containing procedures for making the election has been issued. This IRS is also authorized to issue guidance as regulations or in some other form.



59. The acknowledgment required for the donation of a motor vehicle, boat or airplane must include a statement of whether the donee organization provided any goods or services in consideration of the vehicle. If the sole benefit is intangible religious benefits, the acknowledgment must also include a statement to that effect.
60. An officer or employee of the National Archives and Records Administration may disclose returns and return information disclosed by the IRS upon written request from the Comptroller General of the United States to officers and employees of the General Accounting Office.
61. Third party summons described in IRC Sec. 7609(f) or (g) do not require notice to any person, other than the person summonsed, who is identified in the summons. The notice does not apply to John Doe summons or emergency summons.
62. Indirect distributions made through tiers of CFCs qualify for the temporary deduction for extraordinary cash dividends only if they come from a dividend received by one CFC from another CFC in the same ownership chain. Further, in determining the amount of extraordinary dividends, only cash dividends received during the election year into account.
63. The IRS has been given authority to issue regulations to prevent the related party indebtedness limit. Cash dividends would not be eligible for the deduction to the extent attributable to a direct or indirect transfer from a related party to the CFC.
64. The expense disallowance rule is limited to expenses directly allocable to the deductible portion of the qualifying dividend. Foreign taxes not allowed as foreign tax credits for the qualifying dividend deductible portion do not give rise to income inclusions. The only foreign tax credits that can be used to offset the tax on the dividend are the portion of the credits attributable to the nondeductible portion of the dividend.
65. In determining whether a CFC is a 25% owner of a partnership for purposes of determining whether subpart F foreign PHC income results upon a sale of the interest, constructive ownership rules similar to those under IRC Sec. 958(b) will apply.
66. For purposes of computing its accumulated earnings tax, a foreign corporation can deduct any required subpart F inclusions in income.
67. The penalty for failure to file a required PHC return by a foreign corporation is repealed.
68. A U.S. shareholder treated as owning stock in a lower-tier CFC, owned by a higher-tier CFC must make adjustments. The adjustments apply only for purposes of determining the subpart F inclusion. The adjustments don't apply where the owner of the CFC stock or other property was required to make basis adjustments under IRC Sec. 961(a) or (b). The adjustments must be made to
 - a. The basis of such stock and



- b. The basis of any other CFC stock in which the U.S. shareholder is considered owning
- 69. An overall domestic loss for any qualified tax year is any domestic loss to the extent it offsets foreign-source taxable income for the current taxable year or for any preceding qualified tax year by reason of a loss carryback.
- 70. Taxpayers may elect not to retroactively apply the look-through rule for dividends received from 10/50 companies, for tax years beginning after 12-31-02 and before 1-1-05.
- 71. The definition of foreign base company shipping income in IRC Sec. 954(f) prior to its repeal will remain relevant in the determination of shipping income for purposes of the IRC Sec. 904 limitation on the amount of foreign tax credit available.
- 72. The minimum holding period with respect to the foreign tax credit doesn't apply to foreign taxes on gains and other nondividend income of securities dealers. This exemption doesn't apply to RICs and RIC shareholders.
- 73. Erroneous cross references in the foreign tax credit carryback provisions are corrected.
- 74. Days spent in the U.S. by both exempt individuals (teachers, trainees, students, certain professional athletes, and foreign government-related individuals) and those with medical conditions that arose while they were in the United States, are to be excluded in determining whether the individuals had more than a minimal physical presence in the United States during the 10 years prior to expatriation. This clarification affects the application of the alternative tax provisions of IRC Sec. 877.
- 75. The rules are also clarified concerning when an individual is no longer a U.S. citizen or long-term resident.
- 76. There is now a clarification of coordination for applying the inversion transaction rules. If a foreign corporation is treated as a domestic corporation because of an 80% identity transaction, that foreign corporation will not be treated as a surrogate foreign corporation, meaning that its subsidiaries will not be treated as expatriated entities under the 60-80 percent identity transaction rule.
- 77. Technical and clerical corrections are made to the treatment of operating agreements under the elective tonnage tax regime and the timeliness of an election into those provisions.
- 78. The exception to the FIRPTA rules for capital gain distributions to foreign owners aren't applicable to RICs, but are applicable to REITS. Further, the holding period during which a foreign shareholder may not have held more than a 5% interest in the stock class for which the distribution is made is the one year period ending on the date of the distribution.
- 79. The reporting of property transfers to foreign entities is clarified by correcting a clerical mistake.

