

KATRINA EMERGENCY TAX RELIEF ACT OF 2005

Much-needed tax relief available to victims and those who came to their aid

The Katrina Emergency Tax Relief Act of 2005 (KETRA), which was signed into law on Sept. 23, 2005, is geared mostly toward those who were directly impacted by the disaster. There are, however, a number of provisions that are more broadly applicable, specifically with respect to charitable giving.

What follows is an overview of KETRA's provisions. To learn how they may apply to you, please contact us.

Charitable provisions

Increase in deductibility of cash contributions.

The usual limit of 50% of adjusted gross income (AGI) will increase to 100% of AGI for cash contributions to public charities made from Aug. 28, 2005, through the end of 2005. (See Chart 6 from page 14

of the Guide below. The footnotes have been revised to indicate the new contribution limit.)

Increase in charitable mileage allowance.

To the extent that a vehicle is used for Katrina-related relief efforts, the charitable mileage rate will be 34 cents per mile. This higher rate, computed as a percentage of the standard business rate, is effective for charitable mileage starting Aug. 29, 2005, through the end of 2006. (This new information updates the third paragraph on page 15 of the Guide.)

Additional exemption for providing housing.

Taxpayers may take an additional exemption of \$500 for each Hurricane Katrina displaced person (up to four people) that they provide housing for. The housing must be the taxpayer's

primary residence to qualify, and the exemption may be claimed just once per displaced individual in either 2005 or 2006. Unlike other personal exemptions, this one isn't subject to phaseout rules.

Katrina-related losses

Discharge of indebtedness. Taxpayers may exclude from income any discharge of debt to the extent the discharge is attributable to Katrina-related damage. This is valid for debts discharged after Aug. 25, 2005, through Dec. 31, 2006.

Casualty losses. Individuals who suffer Katrina-related casualty losses aren't subject to the 10% AGI limitation or the \$100 floor for deducting such losses.

AGI LIMITATIONS ON CONTRIBUTION DEDUCTIONS¹

CHART 6

Contribution type	Public charities	Private foundations ²	
		Operating	Nonoperating
Cash and unappreciated property	50% ³	50%	30%
Ordinary income property ⁴	50%	50%	30%
Long-term capital gain property ⁵	30%	30%	20%

¹ For this purpose, adjusted gross income (AGI) is computed without regard to the deduction for charitable contributions and any deduction for a net operating loss carryback.

² An operating foundation spends at least 85% of the lesser of its adjusted net income or its minimum investment return in carrying out its exempt activities. Others not meeting this definition are nonoperating foundations.

³ Under KETRA, 100% for cash contributions made Aug. 28 – Dec. 31, 2005.

⁴ Deduction is generally limited to the property's adjusted basis.

⁵ Generally, the full fair market value of the property is deductible, subject to the percentage limitations.

Data source: U.S. Internal Revenue Code

Retirement plan provisions

Waiver of penalty for early withdrawal.

Katrina victims may take a distribution from their retirement plans — even if they aren't 59½ years old — without penalty. The distribution amount, however, is limited to \$100,000, and the distribution must be made within one year of the declaration of the disaster area.

Repayment of qualified disaster relief

distribution. During the three years following the time an individual takes a qualified disaster relief distribution, that individual may repay the amount and have the repayment treated as if it were a rollover contribution into the account. As such, affected individuals will be able to replenish their retirement accounts without being treated as having made an excess contribution to the account.

Taxability of withdrawals. Individuals who take a qualified disaster relief distribution will, unless they elect otherwise, be treated as having made the withdrawal ratably over a three-year period starting with the year in which the withdrawal is made.

Recontribution of withdrawals. To the extent a withdrawal was made to pay for the down payment on a principal residence in a Katrina disaster area, and it wasn't purchased or constructed as a result of Katrina, individuals may recontribute the withdrawal and thereby avoid the tax that would otherwise be due. The amount must be recontributed no later than Feb. 28, 2006.

Business-related provisions

Donations of book inventories. Businesses can get a deduction for books contributed to qualified charities, but only if the books will be used by the charity for educational purposes. The deduction, subject to other limitations already in the law, is allowed for the lesser of the fair market value or twice the basis of the books contributed and applies to contributions made after Aug. 28, 2005, through the end of 2005.



Donations of food inventories. A similar deduction will also be allowed for contributions of food inventory.

Work Opportunity Tax credit. A new class of targeted group — Hurricane Katrina employee survivor — was created for the Work Opportunity Tax credit. To qualify, the survivor must have lived, as of Aug. 28, 2005, in a Katrina disaster area. This applies to an employee who begins work for an employer anytime from Aug. 28, 2005, through Dec. 31, 2005. In the case of a job at a location within a Katrina disaster area, the hiring period is expanded to the two-year period commencing on Aug. 28, 2005.

Employee Retention credit. Certain employers, located in a Katrina disaster area, whose businesses were inoperable for at least one day as a result of Katrina, qualify for a 40% tax credit on the first \$6,000 of wages paid to eligible employees. Qualified wages include those paid from the time the business first became inoperable until such time as the business resumes significant operations at the location. The credit is available through 2005. ▶