



News Release

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New Tax Law Eases Loss Limitations for Katrina Victims

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WASHINGTON — The Internal Revenue Service today is advising taxpayers who suffered casualty or theft losses as a result of Hurricane Katrina about a recent change to the tax law. A new provision lifts certain loss limitations for Hurricane Katrina victims.

Ordinarily, to figure a deduction for a personal casualty or theft loss, you must reduce the loss by \$100 and also reduce the total of your casualty and theft losses by 10 percent of your adjusted gross income. Only the excess over these \$100 and 10 percent limits is deductible. The new law removes these limits for Hurricane Katrina losses, so that the entire amount is deductible.

To qualify, a loss must be attributable to Hurricane Katrina and it must have occurred after August 24, 2005, in the Presidential-declared disaster area. The \$100 and 10-percent limits still apply to losses that were not caused by Hurricane Katrina.

Like all casualty and theft losses, Hurricane Katrina losses must be claimed as an itemized deduction. If you take the standard deduction you cannot claim them. You cannot claim a deduction for any part of a loss for which you receive or expect to receive insurance or other reimbursement.

Casualty and theft losses are generally deductible only in the year the casualty occurred or the theft was discovered. However, because a Hurricane Katrina loss is a disaster loss, you have the option to deduct it on your tax return for the previous year, 2004. The \$100 and 10-percent limits will not apply to that loss in redetermining your 2004 tax. If you have already filed your 2004 return, the loss may be claimed by filing an amended return, Form 1040X, for 2004.

Claiming the loss on an original or amended return for 2004 will provide you an earlier refund, but waiting to claim the loss on this year's return could result in a greater tax saving, depending on your tax situation for 2005. If you wish to claim the loss for 2004, you generally have until the due date for filing your 2005 return to do so.

You determine your loss for personal use property by first figuring the decrease in its fair market value as a result of the casualty or theft. To do this, you must determine the fair market value of your property both immediately before and immediately after the casualty or theft (counting the value of stolen property as zero). An appraisal is the best way to make

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this determination, but under certain conditions you can use the cost of cleaning up and repairing the property as a measure of the decrease in value. Compare the decrease in fair market value with your adjusted basis in the property. The adjusted basis is typically the cost of the property and any improvements. From the smaller of these two amounts, subtract any insurance or other reimbursement you receive or expect to receive. Generally, you figure your loss separately for each item, but treat real estate used for personal purposes, such as your home, as one item (including the land, buildings, trees and other improvements).

Taxpayers filing or amending their 2004 tax return and whose only casualty or theft losses to personal use property claimed on that return were caused by Hurricane Katrina should write in red ink "Hurricane Katrina" at the top of Form 1040X. They must also attach the 2004 Form 4684, writing "Hurricane Katrina" on the dotted line next to line 11 and entering "0" on lines 11 and 17.

Taxpayers filing or amending their 2004 tax return and who also have casualty or theft losses to personal use property not related to Hurricane Katrina should disregard the caution directing taxpayers to use only one Form 4684, located above line 13, and complete lines 13 through 18 for two Forms 4684. The Form 1040X and the first Form 4684 should be prepared as explained above for Hurricane Katrina losses only. The second Form 4684 should be prepared in the normal manner for all gains and non-Hurricane Katrina losses. If both Forms 4684 have a loss on line 18, they should carry the combined losses from that line to Schedule A (Form 1040), line 19. If there is a gain on line 15 of the second Form 4684, disregard the instruction to enter it on Schedule D, and instead enter on Schedule A (Form 1040), line 19, the excess of the loss from the first Form 4684 over the gain on line 15 of the second Form 4684.

For 2005, Form 4684 is being revised to reflect the new law for Hurricane Katrina losses.

In addition, if your casualty or theft loss causes your deductions to be more than your income for the year you claim the loss, you may have a net operating loss, or NOL. An NOL can be used to lower your tax in an earlier year, allowing you to get a refund for tax you already paid, or it can be used to lower your tax in a future year. You do not have to be in business to have an NOL from a casualty or theft loss. For more information, see Publication 536, *Net Operating Losses (NOLs) for Individuals, Estates, and Trusts*.

For more information on deducting disaster losses, see Publication 547, *Casualties, Disasters, and Thefts*, available on the IRS website (www.irs.gov). Keep in mind that Publication 547 has not been updated to reflect the new law. More information on disaster areas can be found at the Federal Emergency Management Agency (FEMA) website (www.fema.gov/news/disasters.fema).

Taxpayers who have been affected by Hurricane Katrina and have questions can call the special IRS disaster hotline at 1-866-562-5227.