

# BOURGEOIS BENNETT CPAs & CONSULTANTS

## SAFE HARBOR METHODS TO DETERMINE THE CASUALTY LOSS TO YOUR PRINCIPAL RESIDENCE OR PERSONAL BELONGINGS (REVENUE PROCEDURE 2006-32)

The amount of a casualty loss is the lesser of (1) the difference between the fair market value of the property immediately before the casualty and the fair market value immediately after the casualty, or (2) the adjusted basis (cost, including subsequent improvements) of the property. See our memorandum discussing the rules governing casualty losses on our web page.

The first step, therefore, is to determine the reduction in value in the property caused by the casualty. IRS regulations provide two ways to determine this reduction in value. The first way is by having the property appraised before and after the casualty by a qualified appraiser. Alternatively, the cost of repairs to the property damaged is acceptable as evidence of the decrease in value of the property if the taxpayer shows that: (1) the repairs are necessary to restore the property to its condition immediately before the casualty; (2) the amount spent for such repairs is not excessive; (3) the repairs do not cost more than the damage suffered; and (4) the value of the property after the repairs does not, as a result of the repairs, exceed the value of the property immediately before the casualty. In order to use the cost-of-repairs method to determine the decrease in fair market value, the regulations require that the taxpayer *actually make* the repairs rather than rely on estimates of repairs that will be performed in the future or not at all.

Both of these approaches come with problems. First, IRS regulations require appraisals to ignore the overall decrease in market value in an area, a requirement difficult to meet in areas such as Lakeview, with its widespread damage. Second, while the use of repairs is an attractive method to determine a casualty loss from the hurricanes, many taxpayers are finding that

their repairs will not be completed (perhaps, not even begun) before the deadline for filing their 2005 tax returns.

To help taxpayers deal with these problems, the IRS has now issued **Revenue Procedure 2006-32**. This revenue procedure provides safe harbor methods that individual taxpayers may use in determining the amount of their casualty and theft loss deductions for their personal-use residential real property and personal belongings damaged, destroyed, or stolen as a result of Hurricanes Katrina, Rita, and Wilma. Specifically, this revenue procedure provides three safe harbor methods that individuals may use to determine the decrease in fair market value of personal-use residential real property. This revenue procedure also provides a fourth safe harbor method that individuals may use to determine the fair market value of their personal belongings immediately before the 2005 Gulf hurricanes.

The Internal Revenue Service will not challenge an individual's determination of the decrease in fair market value of personal-use residential real property attributable to one of the 2005 Gulf hurricanes if the individual qualifies for and uses one of the safe harbor methods described in the revenue procedure. Furthermore, the IRS will not challenge an individual's determination of the fair market value of personal belongings immediately before one of the 2005 Gulf hurricanes if the individual qualifies for and uses the safe harbor method described in the revenue procedure.

Finally, this revenue procedure requires that if an individual uses the Cost Indexes Safe Harbor Method, described below, the individual also must take into account the value of any no-cost repairs.



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## SAFE HARBOR METHODS (CONT'D)

Use of a safe harbor method described in this revenue procedure is not mandatory. An individual may, instead, use the actual reduction in the fair market value of personal-use residential real property or personal belongings, pursuant to the Income Tax Regulations, if the individual has proper substantiation.

The safe harbor methods provided in this revenue procedure apply only to the circumstances within

**IRS REVENUE PROCEDURE  
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REAL PROPERTY.**

the scope of this revenue procedure and may not be used in any other circumstances.

An individual who suffered a casualty or theft loss for the individual's personal-use residential real property or personal belongings damaged, destroyed, or stolen as result of the 2005 Gulf hurricanes may use the safe harbor methods provided in this revenue procedure in determining the amount of the individual's casualty and theft loss deductions.

*Personal-use residential real property and personal residence* - Personal-use residential real property is defined as real property, including improvements (such as buildings and ornamental trees and shrubbery), that is owned by the individual who suffered a casualty loss, that contains at least one personal residence, and that is not used in a trade or business or in a transaction entered into for profit.

Personal-use residential real property does not include rental property. A personal residence is a single family residence, or a single unit within a contiguous group of attached residential units (for example, a townhouse or duplex), owned by the individual who suffered a casualty loss, and consists of the total enclosed square footage of the residence or single unit, including any enclosed structures attached to the residence or single unit. For example, a personal residence includes a basement and an attached garage, but does not include a deck or screened-in porch. A personal residence does not include a condominium or cooperative unit, or any other property for which the individual who suffered the casualty loss does not own the structural components of the building (such as the foundation, walls, and roof), or owns only a fractional interest in all of the structural components of the building, or a mobile home or trailer.

*Personal belongings* - A personal belonging is an item of tangible personal property that is owned by the individual who suffered a casualty or theft loss and that is not used in a trade or business or in a transaction entered into for profit. For purposes of this revenue procedure, personal belongings do not include a boat, aircraft, mobile home, trailer, or an antique or other asset that maintains or increases its value over time.

A qualifying individual may use any of the three safe harbor methods described in the revenue procedure to determine the decrease in fair market value for personal-use residential real property located in the Hurricane Katrina disaster area, Hurricane Rita disaster area, or Hurricane Wilma disaster

area that was damaged or destroyed as a result of one or more of the 2005 Gulf hurricanes. The three personal-use residential real property safe harbor methods are the Insurance Safe Harbor Method, the Contractor Safe Harbor Method, and the Cost Indexes Safe Harbor Method.

### **INSURANCE SAFE HARBOR METHOD.**

Under the Insurance Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may use the estimated loss determined in reports prepared by the individual's homeowners' or flood insurance company setting forth the estimated loss the individual sustained as a result of the damage to or destruction of the individual's personal-use residential real property from one of the 2005 Gulf hurricanes.

### **CONTRACTOR SAFE HARBOR METHOD.**

Under the Contractor Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may use the contract price for the repairs specified in an itemized contract prepared by a contractor, licensed or registered in accordance with State or local regulations, setting forth the costs to restore the individual's personal-use residential real property to the condition existing immediately prior to the applicable 2005 Gulf hurricane. However, the costs of any improvements or additions that increase the value of the personal-use residential real property above its pre-hurricane value, such as the cost to elevate the personal resi-

## SAFE HARBOR METHODS (CONT'D)

dence to meet new construction requirements, must be excluded from the contract price for purposes of this safe harbor. To use the Contractor Safe Harbor Method, the contract must be a binding contract signed by the individual and the contractor. However, the revenue procedure does not require that the repairs be actually completed by the time the taxpayer files his or her return.

### **COST INDEXES SAFE HARBOR METHOD.**

The third method is the Cost Indexes Safe Harbor method. An individual may use the Cost Indexes Safe Harbor Method if the individual's personal-use residential real property has suffered, in the circumstances described below, (1) a total loss of a personal residence, (2) a near total loss of a personal residence, (3) interior flooding over 1 foot of a personal residence, (4) structural damage from wind, rain, or debris to a personal residence, (5) roof covering damage from wind, rain, or debris to a personal residence, (6) damage to a detached structure, or (7) damage to wood decking:

*Total loss.* A total loss of a personal residence occurs if, as a result of a storm surge or catastrophic prolonged flooding due to breaching or overtopping of a protective levee system during one of the 2005 Gulf hurricanes, any one of the following occurred:

(a) The personal residence either collapsed or is structurally unsound (for example, the structural connections in the personal residence, such as nails and anchor bolts, have corroded as a result of prolonged exposure to salt water (including brackish water) over an extended period of time to

the extent that they compromise the structural integrity of the personal residence);

(b) The state or local government or any political subdivision thereof has ordered that the personal residence be demolished or relocated;

(c) The individual has sold the personal residence to an unrelated party for a price that reflects the fair market value solely of the land on which the personal residence is situated; or

(d) The personal residence sustained damage that satisfies



the definition of near total loss, and the individual has demolished the personal residence.

*Near total loss.* The near total loss of a personal residence occurs if, as a result of a storm surge or catastrophic prolonged flooding due to breaching or overtopping of a protective levee system during one or more of the 2005 Gulf hurricanes, the personal residence sustained severe damage necessitating the removal and disposal of substantially all interior wall frame coverings (including drywall and other wall frame coverings), floorings, electrical lines, ducts, plumbing, and other fixtures. For a personal residence sustaining near total loss, only the wood

frame, rafters, and outside facade of the personal residence remain structurally sound and reusable.

*Interior flooding over 1 foot.* Interior flooding over 1 foot occurs if a personal residence was flooded with salt water (including brackish water) to a height of more than 1 foot as a result of a storm surge or catastrophic prolonged flooding due to breaching or overtopping of a protective levee system during one or more of the 2005 Gulf hurricanes, but did not sustain damage that falls within the definition of total loss or near total loss.

*Structural damage from wind, rain, or debris.* Structural damage from wind, rain, or debris occurs if a personal residence sustained major structural damage to the roof and/or outside wall(s) as a result of wind or windblown debris from one or more of the 2005 Gulf hurricanes that exposed part or all of the interior of the personal residence to rain or debris, requiring substantial renovation of the damaged areas. Substantial renovation requires the removal and replacement of drywall or other wall frame coverings, replacement of trim, and repair and painting of the damaged interior areas of the personal residence.

*Roof covering damage from wind, rain, or debris.* Roof covering damage from wind, rain, or debris occurs if a personal residence sustains damage from wind, rain, or windblown debris to roofing felt, shingles, flashings, fascia, or soffit as a result of one or more of the 2005 Gulf hurricanes.

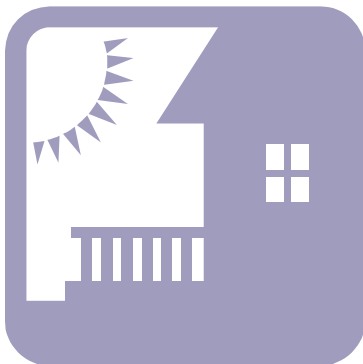
*Detached structures.* A detached structure consists of a detached structure on personal-use residential real property where the detached structure sustained damage from one or more of the 2005

## SAFE HARBOR METHODS (CONT'D)

Gulf hurricanes to the extent that it requires either complete or major rebuilding. A detached structure includes a shed, shop, or detached garage that is not used in connection with a trade or business and that is not equipped with heating or air conditioning. Furthermore, a detached structure is of enclosed wood-frame construction, with some electrical capabilities and little or no interior finishing.

*Wood decking.* Wood decking consists of pressure treated wood decking attached to a personal residence where the decking was damaged or destroyed by one of the 2005 Gulf hurricanes.

Under the Cost Indexes Safe Harbor Method, an individual may use one or more of the cost indexes, as applicable, provided in the revenue procedure to determine the decrease in the fair market value of personal-use residential real property, including the personal residence, detached structures, and wood decking.



Cost indexes are provided for three size categories of personal residences based on the square footage of the personal residence.

In computing the decrease in fair market value under the Cost Indexes Safe Harbor Method, an individual must take into account the value of any no-cost repairs as described later in this memo.

If the Cost Indexes Safe Harbor Method is used, the amount determined is the full amount of the decrease in fair market value of that personal-use residential real property, and it may not be increased by amounts related to items such as landscaping, debris removal, demolition, etc.

The Cost Indexes Safe Harbor Method applies only to the following three types of improvements on an individual's personal-use residential real property: a personal residence, a detached structure, and a pressure treated wood deck. If there is any other type of improvement on an individual's personal-use residential real property, the individual may use the Cost Indexes Safe Harbor Method to determine the decrease in fair market value of the personal-use residential real property, but may not add any amount for the other type of improvements. For example, under the Cost Indexes Safe Harbor Method, no amount may be added to the decrease in fair market value of the personal-use residential real property for a residence that contains a home office, a residence in a structure that contains five or more residential units, a detached structure equipped with heating or air conditioning, or a deck made of synthetic material or hardwood that is not pressure treated.

### **SPECIAL RULES FOR COST INDEXES SAFE HARBOR METHOD.**

(a) A personal residence may not be subject to more than one of the following tables: Table 1 (Total Loss); Table 2 (Near Total Loss); or Table 3 (Interior Flooding Over 1 Foot).

(b) A personal residence subject to Table 3 (Interior Flooding Over 1 Foot) also may be subject to Table 4 (Structural Damage From Wind, Rain, or Debris), but the square footage flooded may not be included in the square footage used for Table 4 (Structural Damage From Wind, Rain, or Debris).

(c) A personal residence subject to Table 3 (Interior Flooding Over 1 Foot) or Table 4 (Structural Damage From Wind, Rain, or Debris) may also be subject to Table 5 (Roof Covering Damage from Wind, Rain, or Debris).

(d) Table 6 (Detached Structures) and Table 7 (Wood Decking) may apply to any personal-use residential real property to which Table 1 (Total Loss), Table 2 (Near Total Loss), or Table 3 (Interior Flooding Over 1 Foot), Table 4 (Structural Damage From Wind, Rain, or Debris), or Table 5 (Roof Covering Damage From Wind, Rain, or Debris) apply.

(e) If an individual's personal-use residential real property contains more than one personal residence and the individual uses the Cost Indexes Safe Harbor Method, the individual must apply the applicable table, or combination of tables, to each personal residence.

**SAFE HARBOR METHODS (CONT'D)**

The following tables set forth the cost indexes for each corresponding category:

<b>COST INDEXES—TOTAL LOSS</b>	
<b>Personal Residence Size</b>	<b>Cost Index Per Square Foot</b>
<b>Small Personal Residence (Less than 1500 Square Feet)</b>	<b>\$175</b>
<b>Medium Personal Residence (Between 1500 and 3000 Square Feet)</b>	<b>\$148</b>
<b>Large Personal Residence (Greater than 3000 Square Feet)</b>	<b>\$132</b>

**Table 1—Total Loss**

For a personal residence that falls within the description of a total loss, use Table 1 as follows:

- (1) Determine the total square footage of the personal residence.
- (2) Determine the size of the personal residence based on the total square footage described in Table 1.
- (3) Multiply the total square footage of the personal residence (from step 1) by the applicable Cost Index in column 2 of Table 1.

**Table 2—Near Total Loss**

For a personal residence that falls within the description of a near total loss, use Table 2 as follows:

- (1) Determine the total square footage of the personal residence
- (2) Determine the size of the personal residence based on the total square footage described in Table 2.
- (3) Multiply the total square footage of the personal residence (from step 1) by the applicable cost index in column 2 of Table 2.

<b>COST INDEXES—NEAR TOTAL LOSS</b>	
<b>Personal Residence Size</b>	<b>Cost Index Per Square Foot</b>
<b>Small Personal Residence (Less than 1500 Square Feet)</b>	<b>\$142</b>
<b>Medium Personal Residence (Between 1500 and 3000 Square Feet)</b>	<b>\$120</b>
<b>Large Personal Residence (Greater than 3000 Square Feet)</b>	<b>\$107</b>

<b>COST INDEXES—INTERIOR FLOODING OVER 1 FOOT</b>	
<b>Personal Residence Size</b>	<b>Cost Index Per Square Foot</b>
<b>Small Personal Residence (Less than 1500 Square Feet)</b>	<b>\$108</b>
<b>Medium Personal Residence (Between 1500 and 3000 Square Feet)</b>	<b>\$ 92</b>
<b>Large Personal Residence (Greater than 3000 Square Feet)</b>	<b>\$ 82</b>

**Table 3 — Interior Flooding Over 1 Foot**

The cost indexes in Table 3 are applied only to the square footage of the personal residence that was flooded, rather than the total square footage.

For a personal residence that was flooded by salt water (including brackish water) to a height of greater than 1 foot and does not fall within the description of a total loss or near total loss this revenue procedure, use Table 3 as follows:

- (1) Determine the total square footage of the personal residence.
- (2) Determine the size of the personal residence based on the total square footage described in Table 3.
- (3) Determine the square footage of the flooded area of the personal residence.
- (4) Multiply the flooded square footage (from step 3) by the applicable cost index in column 2 of Table 3.

**SAFE HARBOR METHODS (CONT'D)**

**Table 4 — Structural Damage From Wind, Rain or Debris**

The cost indexes in Table 4 apply only to the square footage of the damaged area of the personal residence, rather than the total square footage. Personal residences that sustained 100% wind, rain, or debris damage are those that sustained major structural damage throughout the entire personal residence necessitating substantial renovation of all of the rooms in the personal residence.

For a personal residence that sustained structural damage from wind, rain, or debris, use Table 4 as follows:

- (1) Determine the total square footage of the personal residence.
- (2) Determine the square footage of the damaged portion of the personal residence by adding the square footage of each room needing substantial renovation.
- (3) Determine the percent of square footage of the personal residence that was damaged by dividing the square footage that was damaged (from step 2) by the total square footage (from step 1).
- (4) Multiply the square footage of the damaged area (from step 2) by the applicable cost index in column 2 of Table 4 (based on the percent of damage range in column 1 of Table 4).

<b>COST INDEXES—STRUCTURAL DAMAGE FROM WIND, RAIN OR DEBRIS</b>	
<b>Percent of Damage Category</b>	
<b>Percent Damaged = Square Footage of Damaged Area/ Total Square Footage of Personal Residence</b>	
<b>Percent Damaged</b>	<b>Cost Index per Square Foot</b>
<b>15% to 25%</b>	<b>\$143</b>
<b>26% to 50%</b>	<b>\$132</b>
<b>51% to 100%</b>	<b>\$119</b>

**TABLE 5 - Roof Covering Damage From Wind, Rain or Debris**

If the personal residence sustained roof covering damage from wind, rain, or debris, apply the applicable cost index in Table 5 to the total square footage under the roof (including the porch, patios, and overhangs).

For a personal residence that sustained roof covering damage from wind, rain, or debris, use Table 5 as follows:

- (1) Determine the total square footage of the ground floor of the personal residence.
- (2) Add to the total square footage of the ground floor (from step 1) the square footage of any area of the roof that extends beyond the ground floor, such as porches and attached carports, to determine the total square footage under the roof.
- (3) Determine the applicable cost index in column 2 of Table 5 based on the total square footage of the personal residence.
- (4) Multiply the total square footage under the roof (from step 2) by the applicable cost index in column 2 of Table 5 (from step 3).

<b>Cost Indexes—Roof Covering Damage From Wind, Rain or Debris</b>	
<b>Personal Residence Size</b>	<b>Cost Index Per Square Foot</b>
<b>Small Personal Residence (Less than 1,500 Square Feet)</b>	<b>\$6.00</b>
<b>Medium Personal Residence (Between 1,500 and 3,000 Square Feet)</b>	<b>\$5.75</b>
<b>Large Personal Residence (Greater than 3,000 Square Feet)</b>	<b>\$5.50</b>

**SAFE HARBOR METHODS (CONT'D)****Table 6 - Detached Structures**

For a detached structure on personal-use residential real property, apply the applicable cost index in Table 6 as follows:

- (1) Determine the total square footage of the detached structure.
- (2) Determine the size of the detached structure based on the total square footage described in column 1 of Table 6.
- (3) Multiply the total square footage of the detached structure (from step 1) by the applicable cost index in column 2 of Table 6.

<b>COST INDEXES—DETACHED STRUCTURES</b>	
<b>Detached Structure Size</b>	<b>Cost Index Per Square Foot</b>
<b>Up to 200 Square Feet</b>	<b>\$48</b>
<b>Over 200 and up to 400 Square Feet</b>	<b>\$38</b>
<b>Over 400 Square Feet</b>	<b>\$33</b>

**Table 7 - Wood Decking**

For pressure treated wood decking attached to a personal residence, apply the cost index in Table 7 as follows:

- (1) Determine the square footage of the damaged area of the deck.
- (2) Multiply the square footage of the damaged area of the deck (from step 1) by the cost index in column 2 of Table 7.

<b>Cost Index—Wood Decking</b>	
	<b>Cost Index per Square Foot</b>
<b>Use for all sizes of wood decking</b>	<b>\$15</b>

*Example:* The individual's personal residence is substantially damaged by a storm surge from Hurricane Katrina. The individual's personal-use residential real property is located in the Hurricane Katrina disaster area. The damage falls within the definition of near total loss, as defined above, since all of the drywall, floorings, electrical lines, ducts, plumbing, and other fixtures need to be replaced. Prior to Hurricane Katrina, the individual purchased the personal-use residential real property for \$190,000 and spent \$10,000 for improvements to remodel the residence. Immediately prior to Hurricane Katrina, the adjusted basis of the property was \$200,000 (\$190,000 cost + \$10,000 improvements). The personal residence is 2,000 square feet and the personal-use residential real property does not contain any decking or detached structures. The individual paid \$5,000 to have debris cleared from the personal-use residential real property. Insurance and other reimbursements total \$100,000.

Because the damage to the personal residence falls within the definition of near total loss, the individual uses Table 2 of the Cost Indexes Safe Harbor Method to determine the decrease in fair market value of the personal-use residential real property. Using Table 2 of the Cost Indexes Safe Harbor Method, the decrease in fair market value of the personal-use residential real property is determined by multiplying the square footage of the personal residence by the cost index for a Medium Personal Residence as follows: 2,000 sq. ft. × \$120/sq. ft. = \$240,000

Because the individual chooses to use the Cost Index Safe Harbor Method for determining the decrease in fair market value, the \$5,000 debris removal costs are not added to the safe harbor amount of \$240,000. The individual compares the adjusted basis of the personal-use residential real property to the decrease in fair market value determined by using the Cost Indexes Safe Harbor Method. Since the adjusted basis of \$200,000 is less than

## SAFE HARBOR METHODS (CONT'D)

the decrease in fair market value, \$240,000, the individual's casualty loss is limited to the adjusted basis of \$200,000. After subtracting \$100,000, the amount of insurance and other reimbursements received, from the adjusted basis of \$200,000, the individual is entitled to a casualty loss deduction of \$100,000 (\$200,000 - \$100,000 = \$100,000).

*Example:* Winds from Hurricane Katrina caused a tree to fall across a detached garage located on an individual's personal-use residential real property. Prior to Hurricane Katrina, the individual purchased the personal-use residential real property for \$200,000. The personal residence is located in the Hurricane Katrina disaster area. The personal residence is not damaged by Hurricane Katrina. The personal-use residential real property does not contain any decking or other detached structure. The garage suffered significant damage and requires major rebuilding. The total square footage of the garage is 400 square feet. The garage was not insured.

The individual chooses to use the Cost Indexes Safe Harbor Method. Because the garage is a detached structure, the individual uses Table 6 to determine the decrease in fair market value of the personal-use residential real property. Using Table 6, the individual multiplies the total square footage of the garage, 400 square feet, by the cost index of \$38 in column 2 of Table 6: 400 sq. ft. × \$38/sq. ft. = \$15,200

The individual's basis in the personal-use residential real property is \$200,000. The individual compares the decrease in fair market value, \$15,200, with the basis, \$200,000. Since the decrease in fair market value is less than the basis, the individual is entitled to a casualty loss deduction of \$15,200.

A casualty loss must be reduced by insurance or other amounts received, such as amounts given to an individual to repair the damage to the individual's property due to the casualty. This includes the value of repairs to, or rebuilding of, the individual's personal-use residential real property provided by another party at no cost to the individual ("no-cost repairs"), such as the repair or rebuilding of an individual's personal residence by volunteers. No-cost repairs include repairs made for a de minimis or token cost, donation, or gratuity.

An individual who uses the Cost Indexes Safe Harbor Method to determine the decrease in the fair market value of the individual's personal-use residential real property must reduce the loss, determined using the

Cost Indexes Safe Harbor Method, by the value of any no-cost repairs. For this purpose, the value of a no-cost repair is based upon the total square footage completely repaired at no cost to the individual. The total square footage completely repaired at no cost to the individual is multiplied by the same cost index the individual used to determine the decrease in the fair market value of the individual's personal-use residential real property. This amount is then subtracted from the loss determined under the Cost Indexes Safe Harbor Method.

*Certain personal belongings.* Subject to certain exceptions, an individual may use the safe harbor method described below to determine the fair market value of the individual's personal belongings immediately before a 2005 Gulf hurricane in order to compute a casualty or theft loss. If an individual chooses to use the Personal Belongings Safe Harbor Method, the individual must apply that method to all personal belongings for which a loss is claimed except those specifically excluded by the revenue procedure.

To use this safe harbor method, an individual must first determine the current cost to replace the personal belonging with a new one and reduce that amount by 10% for each year the individual owned the personal belonging using the percentages in the Personal Belongings Valuation Table below. If the personal belonging was owned by the individual for nine or more years, the pre-hurricane fair market value is 10% of the current replacement cost under this safe harbor method.

<b>PERSONAL BELONGINGS VALUATION TABLE</b>	
<b>Year</b>	<b>Percentage of Replacement Cost to Use</b>
<b>1</b>	<b>90%</b>
<b>2</b>	<b>80%</b>
<b>3</b>	<b>70%</b>
<b>4</b>	<b>60%</b>
<b>5</b>	<b>50%</b>
<b>6</b>	<b>40%</b>
<b>7</b>	<b>30%</b>
<b>8</b>	<b>20%</b>
<b>9+</b>	<b>10%</b>

## SAFE HARBOR METHODS (CONT'D)

To determine the casualty or theft loss deduction for personal belongings that were damaged, destroyed or stolen:

- (1) Determine the decrease in the fair market value of each personal belonging by subtracting the fair market value of the personal belonging immediately after the hurricane from the fair market value of the personal belonging immediately before the hurricane, determined as described above. If a personal belonging was destroyed or stolen as a result of a 2005 Gulf hurricane its fair market value after the hurricane is zero.
- (2) Determine the basis of each of the personal belongings (generally its cost).
- (3) Compare the decrease in fair market value (from step 1) to the basis of the personal belonging (from step 2). From the lesser of the basis or decrease in fair market value, subtract any insurance or other reimbursements the individual receives or expects to receive for the personal belonging.

*Exclusions.* An individual may not use the Personal Belongings Safe Harbor Method for a boat, aircraft, mobile home, trailer, vehicle or an antique or other asset that maintains or increases its value over time. For purposes of this revenue procedure, a vehicle is an automobile, motorcycle, motor home, recreational vehicle, sport utility vehicle, off-road vehicle, van, or truck.

An individual may determine the pre-hurricane value of a boat, aircraft, mobile home, trailer or vehicle by consulting established pricing sources.

*Example:* An individual's personal belongings included a chair destroyed by Hurricane Wilma within the Hurricane Wilma disaster area. The individual purchased the chair for \$70 four years prior to Hurricane Wilma. The cost to replace the chair with a new chair is \$100. The chair is not insured.

Using the Personal Belongings Safe Harbor Method, the individual computes the fair market value of the chair immediately before the hurricane by multiplying the current replacement cost of the chair, \$100, by the applicable percentage of replacement cost from the Personal Belongings Valuation table, 60%:  $\$100 \times 60\% = \$60$

The individual determines the decrease in the fair market value of the chair by subtracting \$0, the fair market value of the chair immediately after the hurricane, from \$60, the fair market value of the chair immediately before the hurricane.  $\$60 - 0 = \$60$

The individual compares the basis of \$70 to the decrease in fair market value of \$60. Since the decrease in fair market value is less than the basis, the individual is entitled to a casualty loss deduction of \$60.

Disclosure: Individuals who use one of the personal-use residential real property safe harbor methods provided in the revenue procedure should attach a statement to Form 4684, *Casualties and Thefts*, stating that the individual used "Rev. Proc. 2006-32 to determine the individual's Hurricane Katrina, Rita, or Wilma (as applicable) casualty loss deduction and list the specific safe harbor method used, including the table numbers, where applicable (for example, "I/We used Rev. Proc. 2006-32 in determining my/our Hurricane Katrina casualty loss deduction using the Cost Indexes Safe Harbor Method, specifically Tables 3, 6, and 7."). Also, in completing Form 4684, if an individual uses any of the personal-use residential real property safe harbor methods, for each of those properties, do not enter an amount in line 5 or 6 and enter the decrease in fair market value determined under the safe harbor method on line 7 and mark "Revenue Procedure 2006-32" in red ink on the top of the Form 4684.

**BB RECOMMENDS: WE HAVE OMITTED SOME OF THE DETAILED INSTRUCTIONS IN REVENUE PROCEDURE 2006-32. CONSULT YOUR TAX ADVISOR BEFORE IMPLEMENTING IT. IF YOU HAVE ANY QUESTIONS ABOUT THESE NEW RULES OR HAVE OTHER QUESTIONS ABOUT CASUALTY LOSSES OR OTHER STORM-RELATED MATTERS, CALL YOUR BB PROFESSIONAL OR TED STACEY OR KEN FRANZ IN OUR NEW ORLEANS OFFICE.**

**REQUIRED NOTICE IF THIS COMMUNICATION INCLUDES TAX ADVICE: THIS WRITTEN ADVICE IS NOT INTENDED OR WRITTEN TO BE USED, AND IT CANNOT BE USED BY ANY TAXPAYER, FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON THE TAXPAYER.**