

Tax relief for Peace Corps volunteers and employees in the Heroes Earnings Assistance and Relief Tax Act of 2008

Dear Reader,

The recently enacted "Heroes Earnings Assistance and Relief Tax Act of 2008" (the 2008 Heroes Act) contains a wide-ranging package of tax cuts for military personnel and veterans. In addition, a provision in the 2008 Heroes Act will potentially enable more Peace Corps employees and volunteers to qualify for the homesale exclusion on the sale of their principal home. Here are the details of the new provision affecting Peace Corps volunteers.

An individual taxpayer may exclude up to \$250,000 (\$500,000 if married filing a joint return) of gain realized on the sale or exchange of a principal residence. To be eligible for the exclusion, the taxpayer must have owned and used the residence as a principal residence for at least two of the five years ending on the sale or exchange. A taxpayer who fails to meet these requirements by reason of a change of place of employment, health, or, to the extent provided under regulations, unforeseen circumstances is able to exclude an amount equal to the fraction of the \$250,000/\$500,000 that is equal to the fraction of the two years that the ownership and use requirements are met.

There are special rules relating to members of the uniformed services, members of the Foreign Service of the United States, and employees of the intelligence community that allow for an option to suspend the five-year test period for ownership and use during any period these individuals or their spouses serve on qualified official extended duty. This means that they may be able to meet the two-year use test even if, because of their service, they did not actually live in the home for at least the required two years during the five-year period ending on the date of sale. The five-year period can't be extended by more than ten years.

Under the 2008 Heroes Act, a new rule is created for Peace Corps volunteers and certain employees similar to the rules that already apply to the uniformed services, Foreign Service, and intelligence community. Under this new rule, which is effective for tax years beginning after December 31, 2007, an individual may elect to suspend for a maximum of ten years the five-year test period for ownership and use during certain periods that the employee or volunteer is serving outside the U.S.. If the election is made, the five-year period ending on the date of the sale or exchange of a principal residence does not include the period up to ten years during which the taxpayer or the taxpayer's spouse is serving as a Peace Corp volunteer or employee.

For example, let's say that Betty bought and moved into a home in 2002. She lived in it as her main home for two and one-half years. For the next four years, she did not live in it because she was serving outside the United States as a Peace Corps volunteer. She then sells the home at a gain in 2008. To meet the use test, Betty chooses to suspend the five-year test period for the four years she was serving in the Peace Corps. This means she can disregard those four years. Therefore, Betty's five-year test period consists of the five years before she went on qualified official extended duty in the Peace Corps. She meets the ownership and use test because she owned and lived in the home for two and one-half years during the testing period.

I hope this information is helpful. If you would like more details about this provision or any other aspect of the new law, please do not hesitate to call.