CONDON & COMPANY P.C.

Meet Your Ally.

CASUALTY LOSSES

The tax laws allow a deduction for losses of business and nonbusiness property if those losses arise from fire, storm, shipwreck, or other casualty. Damages caused by unprecedented or unusually severe winds or storms, or by hurricanes or tornados ("casualty losses") can be deducted on your tax return.

Regardless of whether a property was used in a trade or business or in a transaction entered into for profit, if the loss arises by reason of a storm or other casualty, then the loss is equal to the lesser of either: (1) the adjusted basis of the property; or (2) the loss of value by reason of the casualty (i.e., the difference between the fair market value of the property immediately before the casualty and the fair market value immediately after the casualty). In addition, the amount of the loss must be reduced by any compensation received from insurance or otherwise.

To substantiate the amount of a casualty loss deduction, you must establish: (1) the adjusted basis of the asset involved; (2) the decline in value of the property as a result of the casualty; and (3) the amount of any reimbursement.

For casualty losses related to personal or family property the deductible loss is much more strictly limited. First, the first $100 of loss from a casualty cannot be deducted. The loss is reduced by $100 per casualty (such as a storm), not $100 per item or $100 per year. Second, after you reduce the amount of the loss by $100, you may deduct only the net casualty loss, i.e., the excess of personal casualty losses for the tax year over the personal casualty gains for that tax year. Third, after applying the first two limits, you may deduct only the portion of the net casualty loss that is greater than 10% of your adjusted gross income. If a casualty involves both real and personal properties, you must calculate the loss separately for each type of property. However, you apply a single $100 reduction to the total loss, then you apply the 10% rule to figure the casualty loss deduction.

Note that a weather-related disaster could actually produce a casualty gain if the property's fair market value, which is later compensated by insurance, is greater than your basis in the property. You may be able to postpone recognizing the gain on your income tax return if you purchase qualifying replacement property that costs at least as much as the payments received for the damaged or destroyed property.

As you can see, the rules regarding the deduction and reporting of casualty losses are very complex, so please contact us to discuss your situation in more detail.

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