

Itemized Deductions Casualty and Theft Losses

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Deductible Losses

Casualty Loss

A casualty loss is the damage, destruction, or loss of property resulting from an identifiable event. The identifiable event must be:

- Sudden, not gradual or progressive.
- Unexpected, not ordinarily anticipated or intended.
- Unusual, not a day-to-day occurrence or typical of the taxpayer's activity.

Casualty and Theft Loss Examples

Deductible	Nondeductible
<ul style="list-style-type: none"> • Blackmail • Burglary • Car accident • Earthquake • Embezzlement • Extortion • Fire • Flood • Hurricane • Kidnapping for ransom • Larceny • Mine cave-in • Robbery • Shipwreck • Sonic boom • Storm • Terrorist attack • Tornado • Vandalism • Volcanic eruption 	<ul style="list-style-type: none"> • Accidental breakage of property under normal conditions. • Burst water heater; however, damage caused by a burst water heater is a casualty. • Car rental while taxpayer's vehicle is repaired. • Costs for protection against future casualties. • Costs for treatment of personal injuries. • Damage caused by a family pet. • Defective design or workmanship that could lead to a collapse or casualty. • Losses caused by willful act or negligence of taxpayer. • Lost money or property. • Normal wear and tear. • Personal use property losses caused by drought. • Progressive damage to property caused by insects or disease. • Sentimental value.

Theft Loss

A theft is the taking and removing of money or property with the intent to deprive the owner of it. The taking of property must be:

- Illegal under the law of the state where it occurred.
- Done with criminal intent.

Deductible Amount of Losses

A nonbusiness casualty or theft loss is the lesser of the taxpayer's basis in the property damaged or destroyed, or the reduction in fair market value due to the casualty or theft. From this amount, any insurance or other reimbursement received, or that could have been received, if the taxpayer chose not to file a claim is subtracted.

The casualty or theft loss is then reduced by \$100 per event when computing the deductible amount. Multiple items lost in a single event result in only one \$100 reduction. The total of all casualty and theft losses from all events during the year is further reduced by 10% of the taxpayer's adjusted gross income.

Criminal Fraud

Victims of criminal fraud or embezzlement related to a transaction entered into for profit are allowed to deduct the theft loss as a miscellaneous itemized deduction not subject to the 2% adjusted gross income limitation. The deduction is also not subject to any other theft loss or itemized deduction reductions or limitations.

Insurance

Losses are not deductible to the extent they are reimbursed by insurance. If property is covered by insurance, a timely insurance claim for reimbursement must be filed or the deduction is not allowed. The part of the loss not covered by insurance is deductible. If a casualty loss is claimed in one year, and in a later year the taxpayer receives reimbursement for the loss, the deductible loss is not recomputed for the taxable year in which the deduction was taken. Rather, the reimbursement amount



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is included in income in the taxable year in which it was received.

Insurance proceeds used for living expenses are not reimbursements for damages so amounts paid for normal living expenses are generally taxable. However, payments to cover a temporary increase in living expenses are excluded from income.

Note: If the casualty occurs in a federally declared disaster area, none of the insurance payments are taxable.

Gain on Reimbursement

If insurance or other reimbursement is more than the basis in the property damaged or destroyed, the reimbursement is a gain. The gain is taxable if a taxpayer does not use the proceeds to purchase replacement property similar or related in service and use.

The gain is postponed if:

- The taxpayer purchases property that is similar or related to it in service or use within two years of the end of the first tax year in which any part of the gain is realized (or acquires at least 80% of a corporation owning such property), and
- The cost of the replacement property is equal to or more than the reimbursement received for the damaged, destroyed, or stolen property.

If the replacement property costs less than the reimbursement, gain is recognized to the extent the reimbursement exceeds the cost of the replacement property.

Federally-Declared Disaster Areas

A federally-declared disaster is a disaster determined by the President to warrant federal government assistance. The 10% of adjusted gross income limitation for casualty losses also applies to the portion of loss due to a net disaster loss.

Year of Deduction for a Federally-Declared Disaster Loss

A taxpayer may elect to deduct a loss in a federally-declared disaster area in the tax year immediately prior to

the disaster year. The return (or amended return) claiming the loss must be filed by the later of:

- The due date for filing the original return (without extensions) for the tax year in which the disaster occurred, or
- The due date for filing the original return (including extensions) for the tax year immediately prior to the tax year in which the disaster occurred.

Items to include on the tax return include the date of the disaster and the city, town, county, and state in which the damaged or destroyed property was located.

Disaster Relief

Food, medical supplies, and other forms of assistance received do not reduce the casualty loss, unless they are replacements for lost or destroyed property. Qualified disaster relief payments received for expenses incurred as a result of a federally declared disaster are not taxable income.

Cash Gifts for Disaster Victims

If a taxpayer receives a cash gift as a disaster victim (such as gifts from relatives and neighbors) and there are no limits on how the taxpayer can use the money, the gift is excluded from income. The casualty loss is not reduced by the cash gift. This is true even if the cash gift is used to help pay for repairs to property damaged in the disaster.

When to Deduct a Casualty or Theft Loss

Casualty or theft losses are deductible in the year the casualty occurred or the theft was discovered. If it is uncertain whether insurance will reimburse all or a portion of the loss, do not deduct the amounts of the loss in question until the tax year when it is reasonably certain the loss will not be reimbursed.

Contact Us

There are many events that occur during the year that can affect your tax situation. Preparation of your tax return involves summarizing transactions and events that occurred during the prior year. In most situations, treatment is firmly established at the time the transaction occurs. However, negative tax effects can be avoided by proper planning. Please contact us in advance if you have questions about the tax effects of a transaction or event, including the following:

- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 70½.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of \$5,000.

This brochure contains general information for taxpayers and should not be relied upon as the only source of authority. Taxpayers should seek professional tax advice for more information.

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