



Disaster and Casualty Losses: Related Tax Rules

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Rural Tax Education

RuralTax.org



- Website hosted by Utah State University
- Material developed, managed, and owned by the **National Farm Income Tax Committee**
- Informational Material on Ag, Timber, and Rural Tax topics include but not limited to:
 - Disaster/Weather Losses
 - Treatment of Government Payments
 - Farm Losses and Hobby Rules
 - Self-Employment Taxes
 - Estate and Gift Taxes
 - Like Kind Exchanges
 - Depreciation
 - Etc...

Program Agenda



Disaster Related
Tax Information
RuralTax.org

- RuralTax.org landing page
- Information including topics such as:
 - Disaster Losses and Related Tax Rules
- Webinars, tax topics, and other resources



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Introduction

- Casualty Losses: Sudden, unexpected, or unusual event (not gradual deterioration)
- Deductible Losses: theft, vehicle or equipment accident, fire (not willfully set), flood, tornado, earthquake, lightning, freeze, terrorist attack, vandalism, volcanic eruption, or government ordered demolition or relocation (condemnation)

The Presentation

- Determining the amount of a loss
- Tax rules that apply
- Examples of business property losses
- Examples of personal property losses
- The need for an asset inventory
- Reconstructing records to prove losses
- References

Extent of Loss

- Compare the Fair Market Value (FMV) of the property immediately before and after the casualty
- The different types of property will have different rules
 - Business use property
 - Raised production
 - Purchased assets (depreciable vs non-depreciable)
 - Cost-share for replacing or repairing
 - Personal use property
- If insured, the proceeds from the insurance policy could result in a taxable gain or a deductible loss

Tax Rules for Business Property

- Business Use Property (look at each item affected)
 - Remaining tax basis (cost less depreciation)
 - Insurance or disaster payment proceeds
 - Casualty gain, elect to replace asset to postpone tax and recognize gain
 - Casualty loss, current tax deduction

Ex. 1: Machinery & Equipment

- Tractor is destroyed
- Adj. Tax Basis = \$99,234 (180,000 cost – 80,766 depreciation)
- FMV before = \$110,000 & FMV after = \$0
- Deductible loss is lesser of:
 - Adjusted tax basis = \$99,234, or
 - Decline in FMV = \$110,000
- If insured for \$100,000, then a \$766 taxable gain
- Buying a replacement tractor for at least \$100,000 results in none of the \$766 gain being taxable

Ex. 2: Machinery Shed

- Shed roof lost due to high winds
- Repair cost to restore shed = \$24,500
- Deductible loss is \$24,500 unless shed was insured.
- If insured and the reimbursement was \$20,000.
 - Deductible loss is \$4,500 ($24,500 - 20,000$)
- If insured and the reimbursement was \$26,000.
 - Taxable gain is \$1,500 ($26,000 - 24,500$)

Ex. 3: Fences

- Fence destroyed by flooding
- Adjusted Tax Basis = \$0 (fences were fully depreciated).
- FMV change does not matter; cost was already deducted.
- Deductible loss is \$0.
- If farmer gets a cost share payment to replace the fence, report the cost share payment as income and deduct the cost of the fence using depreciation.

Ex. 4: Breeding, Dairy, or Draft Animals

- Raised animals have \$0 tax basis.
- Purchased animals may have a tax basis if not fully depreciated.
- If gain occurs from a sale or indemnity payment, gain can be deferred by electing to replace animals.
- A loss is deductible for sales in excess of normal.

Ex. 4: Breeding, Dairy, or Draft Animals (cont.)

- Replacement rules vary depending upon the casualty causing the sale or loss of the animal.
- Diseased animals: condemnation reimbursement = 1 year replacement period with dollar for dollar & head for head requirement.
- Weather related sale: 2-year replacement period and dollar for dollar if outside a federal or state declared disaster area.
- Weather related sale: 4-year replacement period and dollar for dollar if in a federal or state declared disaster area.

Ex. 5 Livestock Purchased for Resale

- Tax treatment: cash versus accrual taxpayer
- Cash basis farmer: cost of animal deducted in the year that the animal is sold, or casualty loss occurs.
- Accrual basis farmer:
 - Loss occurring in year of purchase; deduct the cost of animal.
 - Loss occurring in year after purchase; in the year of purchase the cost of the animal is included in inventory therefore in the year of then loss, a deduction is not allowed.

Ex. 6: Raised Animal for Sale

- Costs of raising the animal are deducted in the year that the expenses of raising are paid.
- The animal will have a zero-tax basis when lost to a casualty event (costs of raising already deducted).
- NOTE: In both examples 5 and 6, the future income that is expected (sale of calves that would have been produced) is not allowed as a deduction.

Ex. 7: Raised Crops, Plants, and Produce for Sale

- Costs of raising the crop are deducted in the year that they are paid.
- The production will have a zero-tax basis when lost to a casualty event.
- The future income that is expected from the sale of the crop is not allowed as a deduction.
- If insured, the indemnity payment is included in income.

Ex. 8 & 9: Stored Feed, Tools, and Supplies

- Cost of these items is deducted as an expense in the year paid.
- The tax basis of these items is zero.
- The casualty will not result in a deductible loss
- If insured, the indemnity payment is included in income.

Tax Rules for Personal Property

- Personal Use Property
 - Prior law required an area to have a federal disaster declaration for a personal property casualty loss to be deductible.
 - **OBBBA:** Now an area can receive either a **federal disaster declaration** or a **state disaster declaration** which allows for a deductible casualty loss.

Tax Rules for Personal Property

- Personal Use Property (look at each item affected separately)
 - Insured or not insured
 - Insurance proceeds
 - Itemized deduction subject to limits
 - Reduce loss by \$100 for each event, then
 - Reduce the previous amount by 10% of the adjusted gross income

Ex. 10: Loss of Home

- Look at the adjusted tax basis and compare to the change in fair market value.
- Adj. Tax Basis = \$207,500 (200,000 cost + 7,500 improvement)
- FMV before = \$250,000 & fair market value (FMV) after = \$0
- Deductible loss is the lesser of:
 - Adjusted tax basis of \$207,500, or
 - Decline in FMV of \$250,000
- Insured for \$185,000, then \$22,500 ($207,500 - 185,000$) is the casualty loss before the itemized deduction adjustment.

Ex. 11: Damage to Personal Vehicle (non-business use)

- Paid \$35,000 for the vehicle
- Adj. Tax Basis = \$35,000 (not a depreciable asset)
- FMV before = \$12,000 & FMV after = \$1,000
- Insurance company paid \$12,000
- Expense to repair vehicle is \$9,000
- Potential gain is \$3,000 ($12,000 - 9,000$), but it is a personal use asset, so no taxable gain.

Ex. 12: Loss of Home Contents

- Need to have the purchase price of items lost to the casualty.
- Compare purchase price to decline in FMV.
- Adjust the smaller of the above amounts by the insurance payment received.
- This amount is then subject to the itemized deduction adjustment.

Ex: Loss of Land

- Need to have the purchase price of items lost to the casualty.
- Compare purchase price or basis to decline in FMV.
- Must have an appraisal to determine FMV before and after the destruction.
- This amount is then subject to the itemized deduction adjustment.

Reconstructing Records



- IRS Pub 2194, Disaster Resource Guide: prescribed methods to reconstruct records
- Likely essential for tax purposes, getting federal assistance, or insurance purposes
- Historical information most likely lost but can be reconstructed for real property, vehicles, machinery, equipment, personal property, business records, etc.

Documenting Losses

- Photographs (before and after loss)
- Inventories (receipts for purchase)
- Tax Records (depreciation schedule)
- Federal or state disaster declaration reports
- Consult your tax advisor as quickly as possible following the casualty or disaster

References

- **RuralTax.Org link to landing page for Disaster Tax Information is**
<https://extension.usu.edu/ruraltax/disaster-tax-info>
- **RuralTax.org: “Disaster Losses and Related Tax Rules” (RTE 2025-10)**
 - Examples for different property or assets
 - How to reconstruct your records
 - List of helpful IRS publications and resources
- **RuralTax.org: “Weather Related Sales of Livestock” (RTE 2025-1)**

Questions and Comments

For any follow-up questions contact:

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