When to Claim a Disaster Loss

Article Highlights:

- Disaster Losses
- Elections
- Net Operating Loss
- AGI Limitations
- Possible Gain

With the wild fires and draught in the West and flooding on the East Coast, we have had a number of presidentially declared disaster areas this year. If you were an unlucky victim and suffered a loss as a result of a casualty, you may be able to recoup a portion of that loss through a tax deduction. If the casualty occurred within a federally declared disaster area, you can elect to claim the loss in one of two years: the tax year in which the loss occurred or the immediately preceding year.

By taking the deduction for a 2015 disaster area loss on the prior year (2014) return, you may be able to get a refund from the IRS before you even file your tax return for 2015, the loss year. You have until the unextended due date of the 2015 return to file an amended 2014 return to claim the disaster loss. Before making the decision to claim the loss in 2014, you should consider which year's return would produce the greater tax benefit, as opposed to your desire for a quicker refund.

If you elect to claim the loss on either your 2014 original or amended return, you can generally expect to receive the refund within a matter of weeks, which can help to pay some of your repair costs.

If the casualty loss, net of insurance reimbursement, is extensive enough to offset all of the income on the return, whether the loss is claimed on the 2014 or 2015 return, and results in negative income, you may have what is referred to as a net operating loss (NOL). When there is an NOL, the unused loss can be carried back two years and then carried forward until it is all used up (but not more 20 years), or you can elect to only carry the unused loss forward.

Determining the more beneficial year in which to claim the loss requires a careful evaluation of your entire tax picture for both years, including filing status, amount of income and other deductions, and the applicable tax rates. The analysis should also consider the effect of a potential NOL.

Ordinarily, casualty losses are deductible only to the extent they exceed $100 plus 10% of your adjusted gross income (AGI). Thus, a year with a larger amount of AGI will cut into your allowable loss deduction and can be a factor when choosing which year to claim the loss.

For verification purposes, keep copies of local newspaper articles and/or photos that will help prove that your loss was caused by the specific disaster.

As strange as it may seem, a casualty might actually result in a gain. This sometimes occurs when insurance proceeds exceed the tax basis of the destroyed property. When a gain materializes, there are ways to exclude or postpone the tax on the gain.

If you need further information on casualty and disaster losses, your particular options for claiming the loss, or if you wish to amend your 2014 return to claim your 2015 loss, please give this office a call.