

## Disaster Losses and Related Tax Rules\*

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### Introduction

The dollar value of property losses due to fires, floods, tornadoes, earthquakes, lightning, freezes, etc. can be substantial. Federal income tax regulations often provide relief by allowing deductions for losses of business-use property. The passage of the Tax Cuts and Jobs Act of 2017 (TCJA) resulted in significant modifications to the deductibility of losses involving personal-use property. In order to deduct a loss for personal-use property as a Miscellaneous Itemized Deduction on *Schedule A (Form 1040), Itemized Deductions*, the area in which the loss occurred must be declared a federal disaster area. The passage of the One Big Beautiful Bill Act of 2025 (OBBBA) made the changes from the TCJA permanent. This fact sheet describes losses to property, the process used to determine if you have a deductible loss, how insurance proceeds and cost share benefits are treated, and how to reconstruct records to document a loss. Examples help explain the rules that apply to property found on the farm including buildings, machinery, livestock, feed, and supplies, as well as the home and its contents and personal vehicles. A list of related Internal Revenue Publications is included at the end of this fact sheet. These publications provide additional information covering disaster losses.

A **casualty** is defined as the damage, destruction, or loss of property resulting from an identifiable event that is sudden, unexpected, or unusual. Therefore, the casualty event must not be gradual or progressive deterioration, an event that is anticipated or intended to occur, or a day-to-day occurrence from an activity in which the taxpayer is engaged. A deductible loss can occur from a vehicle or equipment accident, earthquake, a fire that was not willfully set by the taxpayer, flood, freeze, lightning, hurricane, tornado, terrorist attack, vandalism, volcanic eruption, or government-ordered

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\* This material is based upon work supported by the U.S. Department of Agriculture, under agreement number FSA21CPT0012032. Any opinions, findings, conclusions, or recommendations expressed in this publication are those of the author(s) and do not necessarily reflect the views of the U.S. Department of Agriculture. In addition, any reference to specific brands or types of products or services does not constitute or imply an endorsement by the U.S. Department of Agriculture for those products or services.

demolition or relocation.

To determine the extent of a loss, the owner of the property needs to compare the property's condition immediately before and after the event to determine the extent of the loss and whether the amount may be deductible against taxable income. If the damaged property was insured, there may be the possibility of a taxable gain if the insurance reimbursement is greater than the amount of the deductible loss. This article addresses casualties and the information needed to determine whether or not a taxpayer will have a deductible loss or a taxable gain depending upon the type of property that was damaged or destroyed and if it was or was not insured.

## Farm and Business-Use Property

A farm operator can deduct casualty losses that occur in the business of farming. For a loss to be deductible, a taxpayer must show proof that a casualty occurred. A record must be kept containing a description of the casualty (fire, tornado, etc.) and when it occurred, plus proof that the loss was a direct result of the event. In addition, the taxpayer must have ownership of or be liable for the damage to the property. If the property was insured, there is a need to provide information that there is the possibility for reimbursement for all or part of the loss. The following describes and discusses the damage or destruction of various types of property, both farm business-use and personal-use property. The loss of business-use property is presented first, followed by loss of personal-use property.

### Example 1: Machinery and Equipment

Your combine is completely destroyed. The combine was purchased four years ago for \$180,000 and you took a total of \$80,766 of depreciation. The fair market value immediately before the fire was \$110,000 and zero immediately afterward. Your remaining income tax basis in the combine at the time of the fire was \$99,234 (\$180,000 less \$80,766) and the machine was not insured. Your deductible loss in the year the machine burned is the lesser of the adjusted basis or the decrease in the fair market value. The remaining tax basis of the combine was \$99,234 and the decline in the fair market value was \$110,000. Therefore, the deductible loss is \$99,234.

If the combine had been insured and the insurance reimbursement was greater than the loss, there can be a taxable gain. Assume the amount of the insurance reimbursement for the combine was \$100,000. The taxable gain to be reported is \$766 (\$100,000 insurance reimbursement less the \$99,234 loss). You can avoid reporting the gain by purchasing a replacement combine. If you spend \$100,000 on the new machine, then none of the insurance reimbursement is taxable and the \$99,234 depreciable basis of the old combine plus the \$766 casualty gain becomes the depreciable basis of the replacement combine (\$100,000). In this case, none of the reimbursement is taxable in the year the casualty loss occurred.

### **Example 2: Multipurpose Farm Building**

A tornado takes the roof off your shed that is used to store machinery, equipment, vehicles and farm supplies. After inspecting the building, it is determined that only the roof has to be repaired. The cost of repairing the roof to its condition immediately before the tornado is \$24,500. Therefore, the deductible loss is limited to the cost of the repairs (\$24,500).

If the shed is insured and you received an insurance reimbursement of \$20,000 for the roof repair, your deductible loss would be \$4,500 (\$24,500 less the \$20,000 of insurance reimbursement). Had the reimbursement been \$26,000, then you would have a taxable gain of \$1,500 (\$26,000 of insurance reimbursement less \$24,500 repair cost).

### **Example 3: Fences**

A fire that was a result of an accident burns your pasture and all the fences are destroyed. The fences were completely depreciated and therefore had a zero tax basis. You decide to replace the perimeter fences; you will not have a deductible loss since the tax basis of the fences is zero. The total costs of the fences you replace are depreciable subject to current depreciation rules. The loss of future income from grazing the pasture is not allowed as a deduction. Should you qualify for cost sharing to replace the fencing, the amount of the cost sharing is not taxable, but it will reduce the depreciable basis in the new fence. Here, you do not get a tax deduction, but you also do not have to include the cost share payment in income.

Depending upon the amount of the reimbursement, a *Form 1099-G, Certain Government Payments* will likely be issued to you. Should this occur, you will likely need to report the amount of the proceeds and then offset this with the repair expense. It is important to keep all receipts to document the income and expenses for proper reporting on the income tax return.

### **Example 4: Breeding, Dairy, or Draft Livestock**

The tax treatment of a casualty loss of breeding, dairy, or draft animals is different for raised versus purchased animals. When these animals are raised, all the costs of raising them are deducted as operating expenses on *Schedule F (Form 1040), Profit or Loss from Farming*, and therefore they will have a zero tax basis. Purchased breeding, dairy, or draft animals are depreciable and the loss will be limited to the remaining undepreciated purchase cost. This example explains the loss calculations for both raised and purchased breeding animals. Lightning kills 20 head of raised cows and a bull you purchased. The costs of raising the cows were deducted; therefore, there is no deductible casualty loss. The undepreciated value of the bull was \$1,100; therefore, the deductible loss is the \$1,100 remaining depreciable basis. For additional information refer to the “Weather-Related Sales of Livestock” factsheet which can be found on the RuralTax.org website under the ‘Tax Topics’ tab.

### **Example 5: Livestock Purchased for Resale**

The tax treatment of livestock purchased for resale depends upon whether you report income and expenses using the cash method of accounting, or you use the accrual method of accounting. Cash basis accounting requires that income is reported on the tax return in the year received and expenses are deducted in the year they are paid. However, there is a unique situation concerning the deduction of the purchase cost of the animal(s). The amount paid for the animal is not deducted until the animal is sold. At that time the cost of the animal reduces the income from the sale. Therefore, the total purchase cost of the animal is amount of the casualty loss that is deducted in the year the loss occurs. For example, in October you paid \$600 for a yearling steer to be put on winter pasture and in the following spring lightning kills it. The \$600 purchase cost is the casualty loss that is allowed in the year the animal was killed. The costs of growing the steer (feed, vet expenses, etc.) are deducted in the year they are paid.

If you use accrual accounting, the steer that was purchased would be included in the inventory of animals purchased for resale and removed from inventory in the year that it was sold. Using the same information, in October you paid \$600 for a yearling steer to be put on winter pasture and at the end of the year you put in your tax records the cost of the steer in the end inventory. In the following spring, lightning kills it. The animal is simply removed from the closing inventory for the year of the loss, and you do not get to take a separate deduction since the adjustment is done in the ending inventory. In both the cash and accrual method of accounting, the future income from the animal is not allowed as a deductible loss even though their value typically increases as they grow.

### **Example 6: Raised Livestock for Sale**

The tax treatment livestock of raised for sale is similar to that for breeding, dairy, and draft livestock if you are a cash basis taxpayer. Since the cost of raising an animal is deductible on Schedule F, there is no cost basis for the animal and there is no deductible loss. All the costs of raising the animal are deducted. Like Example 5, the future income from these animals is not allowed as a deductible loss even though their value typically increases as they grow.

### **Example 7: Raised Crops, Plants, and Produce for Sale**

The loss of raised crops for sale is similar to the loss of livestock raised for sale. Since the cost of raising the crop is deductible on *Schedule F (Form 1040), Profit or Loss from Farming*, there is no cost basis for the crop and there is no deductible loss. All the costs for tillage, seed, fertilizer, pesticides, etc. are deducted when paid, so again there is not a deductible casualty loss.

### **Example 8: Stored Feed and Grain**

The loss of feed and other supplies on hand will not create a casualty loss since the purchase cost of these items or the cost of raising the feed or grain is a deductible business expense when paid. Thus, stored hay that was raised to be fed, which was destroyed, will also not create a casualty loss since all the costs of raising and getting it into storage are deductible farm business expenses.

### **Example 9: Tools and Supplies**

The loss of shop tools and other farm supplies will not create a casualty loss since the purchase cost of these items is a deductible business expense when paid. Therefore, their tax basis is zero and the loss will not result in an additional deduction due to the casualty.

## **Personal-Use Property**

As previously stated, the Tax Cuts and Jobs Act of 2017 made significant changes to the allowable deduction of personal casualty losses, which were made permanent by the passage of the One Big Beautiful Bill Act of 2025. An area must receive either a federal disaster declaration or a state disaster declaration in order for personal casualty losses to be deductible as a miscellaneous itemized deduction. The following discussion assumes that a federal disaster declaration applies and the deduction of the losses are allowed.

The following examples discuss loss of or damage to personal-use property and how the loss is calculated. Personal-use property includes items used by you and your family for non-business purposes. Examples of personal-use property include your home, furniture, appliances, electronics, clothing, jewelry, automobiles, and other property that are not used in a trade or business.

To determine the amount of the casualty loss for personal-use property, the following steps are used. Step one, you must determine the adjusted tax basis in the property immediately before the casualty. The adjusted tax basis equals the price paid for the item plus the cost of any improvements made to the property and less any damage to the property. Step two, you must determine the decrease in the fair market value of the property immediately after the casualty occurred. This is the difference between the fair market value immediately before and immediately after the casualty. In many cases, an appraisal will be needed to document this for tax purposes. Finally, you take the smaller of the amounts from either step one or step two and reduce it by any insurance or other reimbursement you receive or expect to receive in the future.

The amount of the loss is then reported as an itemized deduction and subject to two deduction rules that limit the amount of the allowed deduction. First, after having determined the loss following the steps above, reduce the loss by \$100 for each casualty or theft event that occurred during the year.

Second, add all the losses from each event and reduce the total amount by 10 percent of your adjusted gross income (AGI). This amount will be the allowed casualty and theft loss deduction allowed as an itemized deduction. For additional information, refer to *IRS Publication 584, Casualty, Disaster, and Theft Loss Workbook (Personal-Use Property)* which is discussed at the end of this fact sheet. It is important to work with your tax advisor to ensure that you get the correct information and that a loss is computed and reported correctly on the income tax return.

#### **Example 10: Loss of Home**

Your home is completely destroyed. You paid \$200,000 to have the home built, and later added a screened-in room for \$7,500. Before the casualty, your adjusted basis in the home is \$207,500 (\$200,000 plus \$7,500). A recent appraisal was completed on the home and the fair market value was determined to be \$250,000 before the casualty, and since it was completely destroyed, the fair market value after the casualty was zero. It was insured for \$185,000. The amount of the casualty loss allowed is \$22,500 (the lesser of the adjusted basis (\$207,500) or the decrease in the fair market value (\$250,000) less the insurance reimbursement (\$185,000)). The calculation is as follows: \$207,500 adjusted basis less \$185,000 of insurance proceeds equals a \$22,500 casualty loss.

#### **Example 11: Loss of Automobile(s)**

The family car was damaged when a tree fell on it. You paid \$35,000 for it new, so that is the adjusted basis before the casualty as no depreciation is allowed for personal vehicles. The fair market value before the casualty as estimated by a car dealer was \$12,000, and \$1,000 after the casualty (salvage value the dealer was willing to pay for the car). The decline in the fair market value was \$11,000 (\$12,000 less \$1,000). You received an insurance reimbursement of \$12,000, which was used to repair the car to a useable condition. The cost of doing the repairs was \$9,000. Since this was a personal-use asset, there is no taxable gain even though the insurance reimbursement was greater than the cost of repairing the car.

#### **Example 12: Loss of Home Contents**

The process of determining the amount of a casualty for items in the home and other personal-use items requires that the purchase price be compared to the decline in the fair market value of the items before and after the casualty, adjusted for any insurance reimbursement received or expected to be received. The purchase price is compared to the decrease in the fair market value. The smaller amount is then adjusted by any insurance reimbursements to determine the amount of the casualty loss. It will be necessary to create a room-by-room inventory list of items in order to ensure that nothing is missed. The discussion of reconstructing your records later in this article contains suggested methods of determining cost figures for personal-use property.

When a single event, such as a fire or tornado, involves more than one item of property, separate calculations must be made to determine the loss or possible gain for each business-use item and

personal-use item. Once this is completed, then the amounts are combined to determine the overall loss or gain for the business-use property and the personal-use property.

In addition, it is important to keep track of insurance and other reimbursements including disaster relief payments, since these items will impact the amount of the loss that is allowed. If the area is determined to qualify as a federal disaster area, some disaster payments will not be taxable. In addition, if a federal disaster declaration is made, some casualty gains can be deferred if the taxpayer elects to replace the property and does so within the prescribed period of time. The replacement property must be similar to the property that was lost or destroyed to postpone reporting the gain on a tax return. It is also possible to postpone reporting gain if the reimbursement is used to restore, repair, or replace the property. To postpone reporting all the gain, the total amount of the reimbursement must be spent.

To correctly report casualty losses, it is important to have and maintain good records. It is also important to list all property that was damaged or destroyed, including its cost or other tax basis, the amount of insurance or other reimbursements, and the fair market value immediately before and after the casualty occurred. This information is needed for both business-use and personal-use property. It is also important to work closely with your income tax advisor to make sure that you take advantage of all the beneficial tax provisions that apply to casualty losses and the postponement of gain that can occur.

## **Record Reconstruction Tips**

The reconstruction of records is not an impossible task, but it will require time and effort. Much of the following discussion comes directly from *IRS Publication 2194, Disaster Resource Guide for Individuals and Businesses*. It contains the IRS prescribed methods that can be used to reconstruct records. Supplemental information has also been added to assist in locating agricultural-based information as well. Instructions for obtaining a copy of this, as well as other publications, can be found at the end of this article.

Reconstructing records after a disaster will likely be essential for tax purposes, getting federal assistance, or insurance reimbursement. Historical records that you need to prove your loss may have been damaged or destroyed in a casualty. The following tips are designed to help reconstruct your records to prove loss of personal-use or business property.

## **Personal Residence/Real Property**

- Be sure to take photographs as quickly as possible after the casualty to establish the extent of the damage.
- Contact the Title Company, Escrow Company, or bank that handled the purchase of the property to obtain copies of escrow papers and other documents. Your real estate broker may

also be able to help.

- Use the current property tax statement for land versus building ratios, if available; if not available, get copies of recent statements from the county assessor's office.
- Check with appraisal companies to locate a library of old multiple listing books. These can be used for comparable sales information to establish a basis or fair market value using property sales from the local area.
- Check with your mortgage company for copies of any appraisals or other information they may have about cost or fair market value of the property.
- Tax records may be important to have. If these were destroyed, contact your income tax preparer and request a copy of your income tax return.
- When improvements have been made to the property, contact the contractor(s) to see if records are available. If possible, get statements from them verifying their work and cost.
- If a home improvement loan was obtained, obtain paperwork from the institution issuing the loan. The amount of the loan may help establish the cost of the improvements.
- For property that has been inherited, check court records for probate values. If a trust or estate existed, contact the attorney who handled the estate or trust.
- When no other property records are available, check at the county assessor's office for old records about the property. Look for assessed value(s) and ask for the percentage of assessment to value at the time of purchase. This is a rough guess, but a guess is better than no records at all.

## **Vehicles, Machinery and Equipment**

- Various sources exist that provide values for vehicles, machinery, and equipment. Simply use an internet search for car, truck, or farm machinery, and equipment values.
- Contact the car and machinery dealer and ask for a copy of the original sale contract. If not available, give the dealer all the facts and details and ask for a comparable price figure.
- Another option is to use newspaper ads for the period in which the vehicle was purchased to determine cost basis. Use ads for the period when it was destroyed for fair market value. Be sure to keep copies of the ads for your records.
- If you are still making payments, check with your lien holder. The note should contain useful information.

## **Personal-Use Property**

- The number and types of personal-use property may make it difficult to reconstruct records. One of the best methods is to draw pictures of each room of the home. Draw a floor plan showing where each piece of furniture was placed. Then show pictures of the room looking toward any shelves or tables. These do not have to be professionally drawn, just functional.

Take time to draw shelves with memorabilia on them. Do the same with kitchens and bedrooms. Reconstruct what was there, especially furniture that would have held items in the drawers, dressers, and shelves. Be sure to include garages, attics, and basements with a list of items that were contained in each.

- Get old catalogs. These catalogs are a great way to establish cost basis and fair market value. Check the prices on similar items in your local thrift stores to establish fair market value. Walk through the stores and look at comparable items, especially items such as kitchen gadgets. Look for odds and ends you may have had but forgotten because of infrequent use.
- Use your local “advertiser” as a source for fair market value. Keep copies of the issues handy and copy pages used for specific items to put with your tax records file on the disaster.
- Check local newspaper “want” ads for similar items. Again, keep a copy of any you use for comparison with the tax file.
- If you bought items using a credit card, contact your credit card company.
- Check with your local library for back issues of newspapers. Most libraries keep old issues on microfilm. The sale sections of these back issues may help establish original costs on items such as appliances.
- Go to a used bookstore with a tape measure and the diagram of the destroyed property. Measure several rows of used books and count the number of books per shelf. Add up the prices of those books and determine an average cost per shelf. Then count the number of shelves you had in your home and multiply by the average cost per shelf. This will help determine the value of your books before the loss.

## **Business Records**

- To reconstruct supply inventories, get copies of invoices from suppliers. Whenever possible, the invoices should date back at least one calendar year.
- For income items, get copies of bank statements. The deposits should closely reflect what the sales were for any given time period.
- Obtain copies of last year’s federal, state, and local tax returns including sales tax reports, payroll tax returns and business licenses (from city or county). These will reflect gross sales for a given time period.
- For furniture and fixtures, it will likely be helpful to sketch an outline of the inside and outside of the business location. Then start to fill in the details of the sketches, such as where various equipment and other stored items were located.
- If you purchased an existing business, go back to the broker for a copy of the purchase agreement. This should detail what was acquired.
- If the building was constructed for you, contact the contractor for building plans or the county/city planning commissions for copies of any plans.

For individual assistance, as well as additional information, contact the IRS Disaster Assistance Hotline at 1-866-562-5227. IRS personnel may be able to provide face-to-face assistance covering disaster related issues at your local IRS office or Taxpayer Assistance Center. To find a Taxpayer Assistance Center in your area, go to this website: <http://www.irs.gov/localcontacts/index.html>.

## IRS Publications

The Internal Revenue Service (IRS) has a variety of publications available to assist property owners who experience disasters. The following publications will be quite useful and can be accessed by going to [www.irs.gov](http://www.irs.gov) and clicking on “Forms and Publications”. Then click on “Publication number” under “Download forms and publications by:” Type the publication number in the find box to search for the publication. Publications may be viewed online or downloaded by double clicking on the publication as it appears in the list.

- **IRS Publication 2194, Disaster Resource Guide for Individuals and Businesses.** This publication includes a discussion of disaster resources and assistance available and the process for reconstructing your tax records.
- **IRS Publication 547, Casualties, Disasters, and Thefts.** This publication explains the tax treatment of casualties, thefts, and losses. The publication discusses the following topics:
  - Definitions of a casualty, theft, and loss on deposits
  - How to figure the amount of your gain or loss
  - How to treat insurance and other reimbursements you receive
  - The deduction limits
  - When and how to report a casualty or theft
  - The special rules for disaster area losses
- **IRS Publication 584, Casualty, Disaster, and Theft Loss Workbook (Personal-Use Property).** The workbook is designed to help you create a list of personal-use property that was damaged or destroyed. It contains a variety of schedules with lists of items to help you document various household items on a room-by-room basis as well as other personal-use assets. It will be useful to figure the loss to your main home, its contents, and your motor vehicles.
- **IRS Publication 584-B, Business Casualty, Disaster, and Theft Loss Workbook.** This workbook is designed to help you create a list of business-use property that was damaged or destroyed. It contains a variety of schedules with lists of items to help you document various business-use items. It will be useful to figure the loss on business-use and income-producing property.

- **IRS Publication 225, Farmer’s Tax Guide.** The “Casualties, Thefts, and Condemnations” chapter provides extensive detail concerning damage or destruction to farm property. The examples and discussion focus on casualty loss calculations and tax treatment for various types of farm property and the specific rules that apply.

Due to the complex nature of the casualty loss rules, it is important to work closely with your tax advisor. A trained tax professional can assist by making sure that you properly document your losses and take advantage of all the potential income tax benefits to reduce the adverse economic impact of the casualty. In addition, special rules apply to federally-declared disaster area losses, and your tax professional can help explain these rules help you take advantage of them.

## **Additional Topics**

This fact sheet was written as part of Rural Tax Education, a national effort including Cooperative Extension programs at participating land-grant universities to provide income tax education materials to farmers, ranchers, and other agricultural producers. For a list of universities involved, other fact sheets and additional information related to agricultural income tax please see RuralTax.org.

Fact sheets that might be of interest include

- Weather-Related Sales of Livestock
- Involuntary Conversion of Business Assets
- Sale of Business Property

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This information is intended for educational purposes only. You are encouraged to seek the advice of your tax or legal advisor, or other authoritative sources, regarding the application of these general tax principles to your individual circumstances. Pursuant to Treasury Department (IRS) Circular 230 Regulations, any federal tax advice contained here is not intended or written to be used, and may not be used, for the purpose of avoiding tax-related penalties or promoting, marketing or recommending to another party any tax-related matters addressed herein.

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