



Your Insurance & Recovery Questions Answered

Financial Decision-making & Casualty Loss Taxes

Roadmap to Recovery Q&A

March 25, 2021

2020 CA Wildfires

About United Policyholders (UP)

- Helping disaster survivors and advocating for insurance consumers since 1991
- A trusted information resource and respected voice for insurance consumers in all 50 states
- 30 year track record and expertise in disaster recovery
- Not for profit...not for sale
- Funded by donations and grants

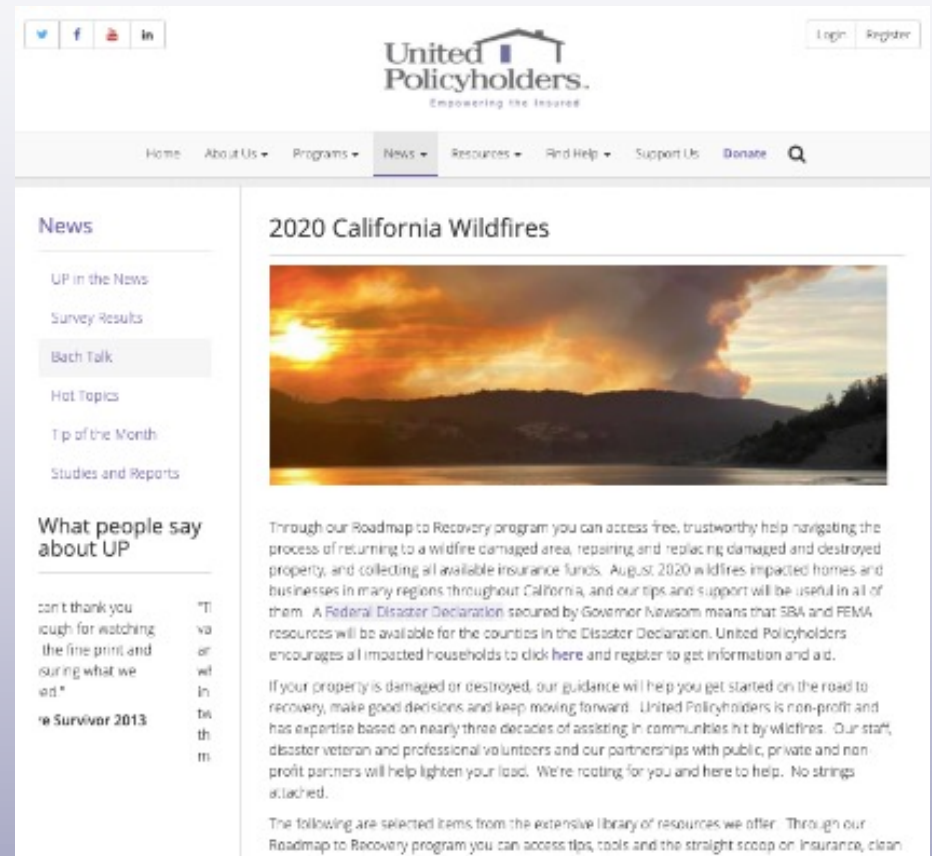
Team UP

- Professional staff
- Government and nonprofit partners
- Volunteers
 - Previous catastrophic loss survivors
 - Consumer-oriented professionals
 - Damage and repair/rebuild cost estimators
 - Lawyers
 - Public Adjusters
 - Tax and Financial Planning experts
 - Construction and Real Estate professionals

Your California Wildfire Help Library

www.uphelp.org/2020Wildfires

- California Specific Resources with Step by Step Guidance
- One Click Links to Sign UP for Events And Email Notifications
- Links to Pro-consumer Professional Help www.uphelp.org/findhelp
- Sample Letters & Claim Forms www.uphelp.org/samples
- Survivors Speak Tips www.uphelp.org/survivorsspeak
- Upcoming Workshops And Resources www.uphelp.org/events



The screenshot shows the United Policyholders website. The header includes the logo "United Policyholders. Empowering the Insured" and navigation links for Home, About Us, Programs, News, Resources, Find Help, Support Us, and Donate. A search icon is also present. The main content area features a "News" sidebar with links to "UP in the News", "Survey Results", "Bach Talk", "Hot Topics", "Tip of the Month", and "Studies and Reports". The main article is titled "2020 California Wildfires" and includes a photograph of a wildfire. The text of the article discusses the Roadmap to Recovery program, a Federal Disaster Declaration, and the availability of SBA and FEMA resources. It also mentions that United Policyholders encourages impacted households to click here and register to get information and aid. A quote from a survivor is partially visible on the left side of the article.

The Fine Print

- This workshop is intended to be general guidance only, not legal advice
- If you have a specific legal question, we recommend you consult an experienced attorney
- We do not endorse or warrant any of the sponsors or the speakers at our workshops
- We are not creating a professional/client relationship with any individual



Today's Panelists

Valerie Brown

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Eileen Freiburger, CFP®

Partner, Abacus Wealth Partners

John Trapani, CPA

John Trapani, CPA, California

Valerie Brown



- **Senior Program Officer, Roadmap to Recovery™**
- **14 years experience in disaster recovery**
- **Officer and Board Member, Disaster Leadership Team**
- **Officer and Board Member, National Aging in Place Council**
- **President, San Diego VOAD**
- **Red Cross and CERT Volunteer**
- **Home Ignition Zone Instructor**

Eileen Freiburger, CFP®

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John Trapani, CPA

- Licensed in California and Colorado
- Disaster survivor
- 27 years of disaster tax reporting
- Has conducted professional seminars to educate fellow CPAs since 2008
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Recap: What do I need to know NOW?

Consider requesting a “Filing Extension” before the deadline to file for your 2020 return. (May 17th, 2021)

File your return or extension timely and report what you know - Don’t rush to claim a “Casualty Loss” as it may turn out to be a **“Casualty - Involuntary Gain”**.

Special IRS rules apply depending on whether there is a Federal Disaster Declaration for your fire – **only (DR) designations qualify.**

While this information is tax related, no final decision about rebuilding or replacing should be based **solely** on tax considerations. **Look at the big picture and your overall financial strategies.**

Why file an extension with the IRS?

- **When in doubt, file an extension....**
- The rules around disaster and tax regulations are complex....
- There are many provisions to help offset the potential tax implications, but it takes time to know the full extent of any potential outcomes....
- Disaster declarations can lag behind and do not always happen by the IRS filing deadlines.....
- It can take several years to know the full extent of the possible tax implications.....
- <https://uphelp.org/claim-guidance-publications/tax-information-for-disaster-survivors/>

In what tax year should I claim a loss?

- Generally, losses can only be deducted in the year in which the loss occurs – this cannot be known until claim is settled.
 - For losses that occurred due to a federal disaster declaration (DR), you can elect to take the loss on an original or amended return for the year preceding the year of loss.
 - For 2020 losses, you have until October 15, 2021, to elect if you would like to claim the loss on an amended or original 2019 return or simply claim the loss on your 2020 return.
- The IRS recently issued Revenue Procedure 2016-53 (<https://www.irs.gov/pub/irs-drop/rp-16-53.pdf>) liberalizing the period available for taxpayers to claim a Code Section 165(i) deduction.

Does my fire have a “Presidential Federal Disaster Declaration (DR)”?

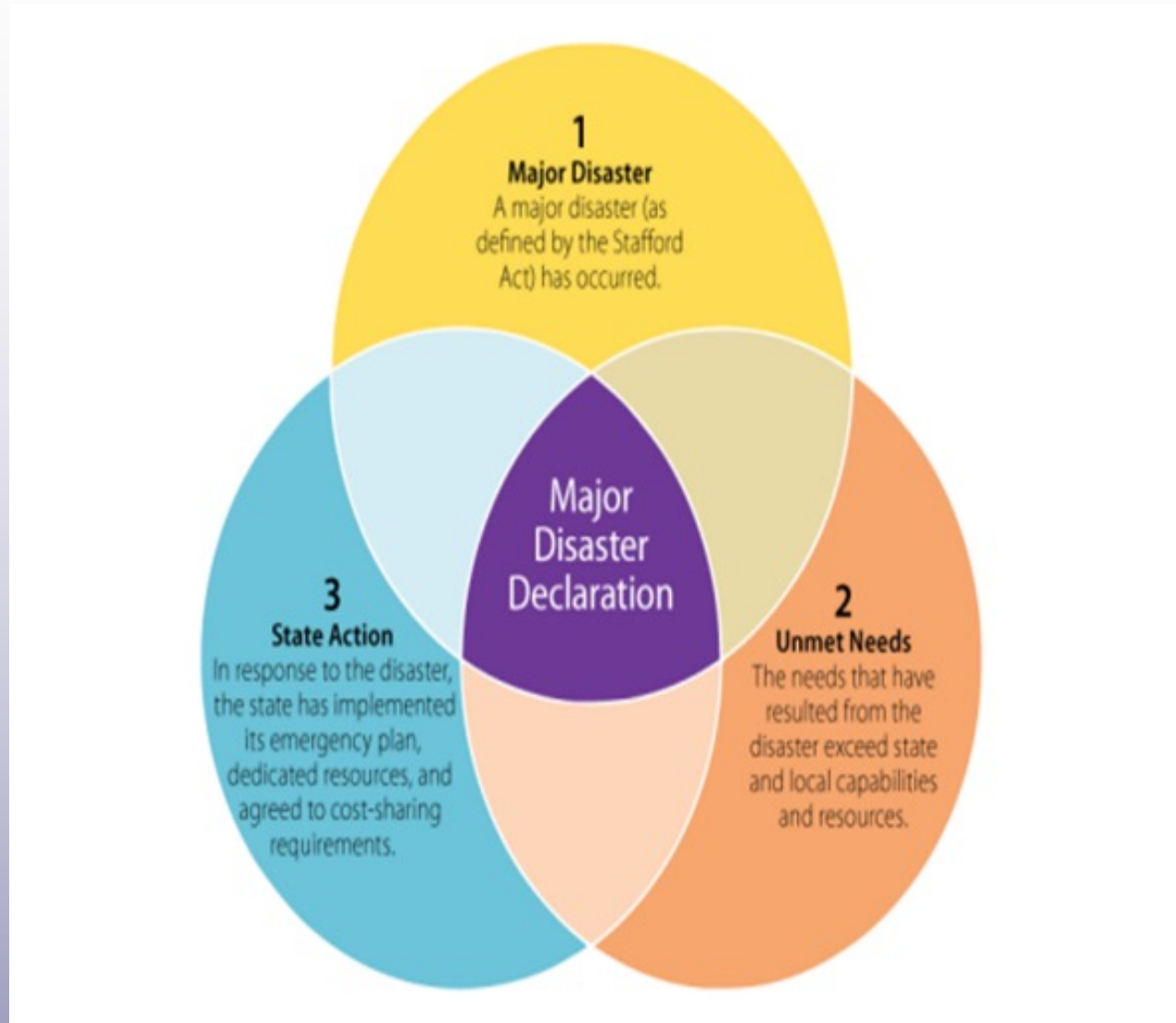
Only Presidential Federal Disaster Declarations (DR) are recognized by the IRS as qualifying.

- <https://www.fema.gov/disasters/disaster-declarations>
- <https://www.irs.gov/newsroom/around-the-nation>

Added provisions available:

- Contents related proceeds for damaged or destroyed property related to a primary residence are not subject to taxation, even when cause a **gain** or potential gain (safe harbor).
- Contents related losses can be considered (added in) when calculating deductions for “**casualty losses**” (*as defined by IRS*).
- Additional time may be allowed for replacing items and extended timelines for certain tax filings.

Major Disaster Declaration (DR-4569-CA and DR-4558-CA)



If I'm underinsured, do I automatically have a loss for tax purposes?

- No, because you may have actually had a gain (in the IRS's view) if you paid less for your home than the amount of your dwelling claim payment.
- Your fire needs a **Federal Disaster Declaration** for you to be able to claim a "**Casualty Loss**" on your tax return.
- Your insurance loss is calculated differently than your dwelling's "**Cost Basis**" to determine a "**Casualty Tax Gain/Loss**".
- You may be subject to a "**Gain**" if your insurance proceeds/payments are greater than the "**Cost Basis**" of your property.
- There are ways to "offset" and/or "convert" these gains.

Q1. Legal / Litigation proceeds

- I was told last year that money I received from the Wildfire Assistance Fund related to the Camp Fire was taxable because that fund was set up by PG&E and PG&E was reporting it. Is that correct? [MM]
- Please discuss specifically taxability of any litigation gain from Camp Fire against PG&E. [MM]

Q2. Litigation settlements

- I had an older mobile home totally with no insurance. Replacing it will cost more than 3 times what it cost 32 years ago. What of the different types of settlements will be taxable, in your experience?
 - home replacement
 - items in the home
 - pain and suffering
 - landscaping
- Also, if you have any knowledge what percentage of 4 taxable types might I have to pay? Will the trust give us a breakdown of how much of each of the 4 types they are giving us so we can do our taxes? [DB]

Legal / Litigation proceeds

- Generally, all non-physical injury claims and loss of income proceeds are considered taxable.
- Compensation for medical care and bodily injury are not taxable.
- The written terms of the settlement/disposition of the lawsuit are what determines whether proceeds are taxable.
- It can take years for these actions to play out to a final outcome.

Q3. FEMA aid & taxes

- I understand that assistance for a FEMA declared disaster no matter the source is not taxable. If the latter is true, what should I give my CPA on this topic?

Which payments **MAY** be taxable by IRS?

For those impacted by a disaster loss regardless of disaster declaration, taxable reimbursements will include:

- Unemployment compensation
- Reimbursement for items already reimbursed (double)
- Payments for real estate are treated the same as if they are proceeds paid by the insurance company
- Some ALE insurance proceeds, if used to purchase an asset rather than to pay for temporary living expenses
- Some Insurance proceeds related to contents, also contents in a second home, even if a (DR)

Which payments are not considered taxable by the IRS?

For those impacted by a disaster loss regardless of declaration, non-taxable reimbursements may include:

- Payments for ALE or Additional Living Expenses (to the extent they are being used to pay for additional living expenses) including insurance proceeds and FEMA payments
- Payments from social welfare agencies, charitable organizations, and in-kind services such as free meals, medical supplies, and shelters are generally not taxable
- FEMA payments under authority of Code Section 139

Q4. Tax implications from losing a “second home”

- I lost a "second home" in a total casualty loss/federal disaster in Healdsburg, CA in 2020. What are my federal and California tax implications on receipt of insurance proceeds and how do they differ than if the house was my primary residence? For example, are my insurance proceeds from personal property recovery excluded from taxation or included? How long do I get to rebuild a house to defer the gain, if I have one? [WL]

Q5. Cost Basis

- I thought I understand that determining the cost basis for the house was the purchase price paid, including cost of the land. Is that correct, even though I still own the land?
- If I spend a portion of my insurance funds on replacement but with a lower cost home, do I subtract the replacement costs I paid, including landscaping, from my insurance gain, before calculating capital gains to be taxed? [DE]

How is “Cost Basis” calculated for IRS purposes?

- “Purchase cost” or “inherited cost” is used, **not market value**
- Certain upgrades and additions can add to the “cost basis”
- “Integral nature” rule for personal use real estate (land, fences, home combined) can accelerate or be combined and added to your cost basis

Disaster Casualty Loss Reporting

2	Cost or other basis of each property ...	2	421,801
3	Insurance or other reimbursement (whether or not you filed a claim) (see instructions)	3	103,555
<p>Note: If line 2 is more than line 3, skip line 4.</p>			
4	Gain from casualty or theft. If line 3 is more than line 2, enter the difference here and skip lines 5 through 9 for that column. See instructions if line 3 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year.....	4	
5	Fair market value before casualty or theft	5	775,000
6	Fair market value after casualty or theft.....	6	100,000
7	Subtract line 6 from line 5.....	7	675,000
8	Enter the smaller of line 2 or line 7.....	8	421,801
9	Subtract line 3 from line 8. If zero or less, enter -0-..	9	318,246
10	Casualty or theft loss. Add the amounts on line 9 in columns A through		
11	Enter the smaller of line 10 or \$100,000		

A qualified personal “casualty loss” is the lesser of?

- The “**Cost Basis**” of the damaged or destroyed property reduced by all insurance reimbursements, payments and proceeds OR
- The decline in “**Fair Market Value**” using before and after the casualty reduced by all insurance reimbursements, payments and proceeds
- It is very rare to end up with a qualified casualty loss do to these rules

Q6. Establishing cost basis

- I and 300 of my neighbors in the CZU complex fire lost homes that were unpermitted. Most of us built our own homes. I kept receipts, but they have now burned. How do we establish a cost basis? Can we value our own labor in the construction? [GR]
- Sweat equity

Q7. Paying off mortgage

- Our insurance originally paid us the full policy amount for the dwelling. We were planning to rebuild. The insurance check payment was made out to both us and the mortgage company. Do I need to pay off the mortgage?
[SS]

Q8. Interest on capital gain

- Are the insurance gains charged 3% interest per year if I don't pay the capital gain in the year I received the insurance payment? My insurance was very efficient and paid me the full amount in 2020, yet I am spending funds now, in 2021, on recovering my land and putting a smaller home on the land (a tiny home). I don't want to be charged 3% interest, so would plan on estimating what my replacement costs will be in 2021, subtracting this amount from the insurance proceedings, but then paying the capital gains on the remaining gain with my 2020 taxes. [DE]

Q9. When to file Form 4684

- Who is required to file tax Form 4684? I'm certain I don't have a tax-deductible loss -- my coverage is adequate enough to cover my loss. I'm also using all of my insurance proceeds to rebuild. Do I need to file Form 4684? Do insurer's send out 1099's reporting settlement payments to the IRS? [VS]

Q10. Extensions & landscaping

- We received the maximum for our landscaping but have not yet replaced it. Do we file for an extension to cover the time it will take to do the work so that we do not have to pay taxes on that money? How long an extension can we request if our loss was landscaping and other structures, not our residence? [MA]

Deep Breath



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Q11. Losses & landscaping

- The insurance company said we might be able to take a loss on our taxes for the additional landscaping and other structures damage they did not cover. Is that a possibility? What would we need to do to prove that loss?

Q12. Timber losses

- My 20 acres is zoned Timber Production. In the 40 years that I have owned it, the value of the trees (for lumber) had increased. But now they are all burned. My homeowners insurance will not cover the timber loss. Is there any way I can recover this in taxes? [GR]
- Cost to remove trees post-fire as the cost basis?

Q13. Prop 19

- In November of 2020, the State of California voters passed Prop. 19, providing a tax savings for those of us who lost our homes in wildfires. My concern is whether this proposition is retroactive to the Paradise Camp Fire of 2018. I know that during the campaign, pro Prop 19 ads featured people from Paradise as a way of getting voters to pass it. [JB]

Q14. What about construction loans?

- Our insurance company paid the policy amount, which left us underinsured. However, my contractor and the insurance company agreed on the cost to rebuild our home, and will pay our extended coverage. Insurance states I must pay my contractor the loan funds already dispersed to us before we are eligible for the additional funds. We used most of to pay off our mortgage.
- Looking at construction loans, we have to qualify for the full house cost minus the balance of funds left. There is NO way we can qualify for that, so we are scrambling to come up with the funds.
- Is there a better way to do this or a way to borrow just the amount from the first insurance payment that we used to pay off the mortgage? I don't know what to do. [SS]

Q15. Selling my lot

- "What if I sell my lot 2 years after the fire, can I still use my exclusion?" / "If I sell my lot will the proceeds be taxable?" So if, as in the most common situation, we are under-insured and receive insurance proceeds that exceed our cost basis, thereby creating an involuntary gain, and we pay capital gains taxes using Schedule D for the structure, what is the subsequent tax treatment if we sell our lot later? [MB]

Lot/Land Sales

- Subject to involuntary gain “**exclusion**” regulations up to \$250,000 single or \$500,000 couple (IRC 121)
- Tax liability can be deferred under (IRC 1033) (Rev. Rul. 96-32) as long as w/in qualified dwelling replacement periods of 4 years with a (DR), or 2 years without
- Replacement period timeline begins when the proceeds are received, not the date of the disaster
- “Integral nature” rule for personal use real estate (land, fences, home combined) can accelerate or be combined and added to your cost basis

Q16. Selling the land – capital gains

- If we decided to sell the land, do we have 3 years from the date of the fire in term of capital gains (primary residence 2/5 years)? [MM]

How long do I have to replace property to use the tax exclusions (IRC121) on my Involuntary Conversion gain?

- Deadline is four (4) years for primary, personal residence in “**Federal Disaster Declarations**” (DR).
- Deadline is two (2) years for all others.
- “**Extensions**” may be available and must be filed.

Note: Replacement period time limits of the 2 or 4 years from the date the *proceeds are received* must be followed or formally extended.

Q17. Selling the land because can't afford to rebuild?

- What are the tax implications if a person has to sell their property because they didn't have enough funds to rebuild? Do they have to pay capital gains tax on the land sale or can they roll the funds into the purchase of a replacement home? What happens if the wildfire loss, the insurance payouts and land sale happen in different tax years? [CL]

Q18. What about taxes and partial loss

- Could you please address how tax issues might differ for a partial loss vs. total?
i.e. major damage to outbuilding but home intact. Also compromised property value if not rebuilding that structure but just repairing. [GR]

Q19. Contents Loss

- If the insurance company estimates our contents loss above the limits of our policy, is that a potential tax write-off? Does cost basis apply in this case? [MM]

Deep Breath



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Q20. Home office/business losses

- Are home office losses a business loss, and where can I deposit building funds to avoid the 2 year rebuilding window? This cannot be done in 2 years. [BW]

Are business related losses taxed differently than personal losses?

Gain/Loss on involuntary conversion calculation is similar to personal property with the following differences:

- Land is not included (unless land is sold due to it no longer being economically viable to owner)
- For complete destruction, no appraisals are needed
- No exclusion on gain available
- Deduction not limited by 10% of AGI and \$100
- Only consider adjusted basis in computing gain or loss not change in FMV
- Loss must be substantiated, similar to individual losses
 - inventory

Can I defer a gain for a business involuntary conversion?

- If the gain results from proceeds in excess of “**Cost Basis**” for your business, you treat the reimbursements as sales proceeds
- You have two years after realizing a gain to reinvest in a property similar or related in service, or use in repairs/rebuilding the damaged/destroyed property

Note: Fed. Dis. Dec. matters

Q21. Determining value of loss

- How do you get an after fire value of your total loss property when there are no other listed or sold parcels to assess value with?
[MP]

Do I have a qualified “Casualty Loss”?

- Probably not, it is very rare that this is established, documented and qualified
- Other provisions of the disaster tax code can be of assistance in reducing any potential tax burden – good news not bad

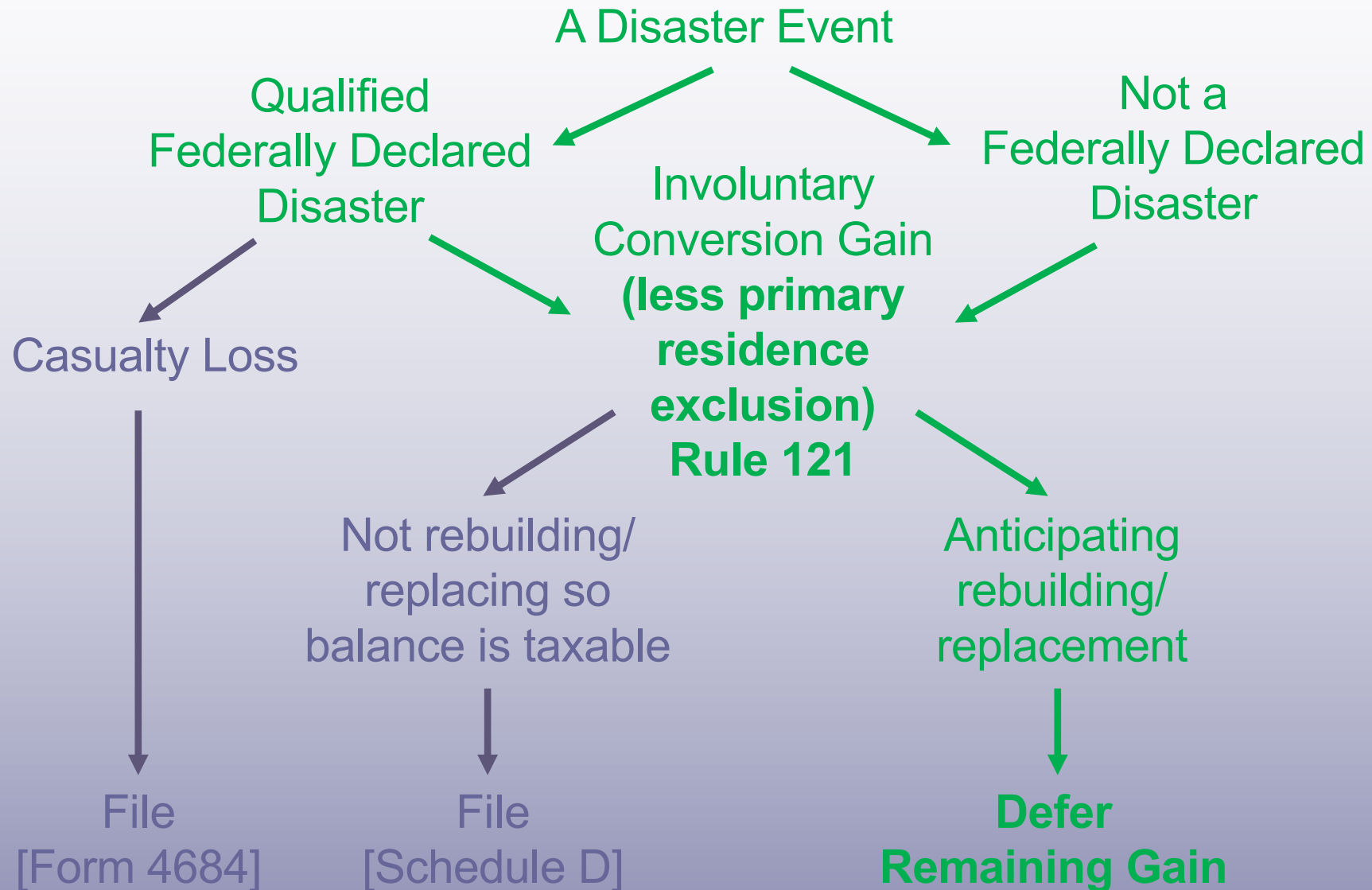
Path to an IRS **qualified casualty loss** for a personal use primary residence?



Do I have an IRS taxable gain?

- It is very possible, especially if your home was purchased many years ago and values have risen.
- You can have a gain, even if underinsured.
- IRS regulations provide help to “offset” or “defer” gains from “involuntary conversions”.
- There are ways that you can reduce the taxable gain while following the regulations.

Path to **offset a gain from proceeds** for a personal use primary residence?



Principal residence was purchased for \$150,000, and \$25,000 was subsequently spent on improvements. The home was destroyed and, instead of rebuilding, the taxpayer purchased a new home for \$275,000 and retained the lot.

Involuntary Conversion (IRC 121)

Insurance proceeds		\$ 800,000
Basis of principal residence destroyed		(175,000)
Realized gain		<u>\$ 625,000</u>
Insurance proceeds		\$ 800,000
Principal residence exclusion (MFJ)		(500,000)
Proceeds realized from involuntary conversion		<u>\$ 300,000</u>

Gain of \$25,000 is taxable in the year the last \$25,000 of proceeds is received.

Proceeds realized from involuntary conversion	\$ 300,000
Basis of principal residence destroyed	(175,000)
Realized gain on involuntary conversion	<u>\$ 125,000 (A)</u>
Proceeds realized from involuntary conversion	\$ 300,000
Cost of new principal residence	(275,000)
Recognized gain	<u>\$ 25,000 (B)</u>
Deferred gain (A - B)	<u>\$ 100,000</u>
Cost of new principal residence	\$ 275,000
Less deferred gain	(100,000)
Basis in replacement property	<u>\$ 175,000</u>

If I have a gain, can I defer it ?

- An “Involuntary Conversion **Gain**” may occur if payments/reimbursements exceed the “**Cost Basis**” of the property
- For personal, primary residences, it may be possible to utilize an “**exclusion**” to offset the gain under sale of personal residence rules (IRC Section 121)
- It is possible to defer the gain if reimbursements are reinvested in rebuilding home or to acquire a **replacement** home or homes within four years if in a “**Federal Disaster Declaration**” (DR) or **2 years** if it is a **second home or not a (DR)**

What are the rules for using the primary residence exclusion (IRC 121)?

- You may exclude up to \$250,000 per individual or \$500,000 per married couple of an Involuntary Conversion **Gain**” on a Personal Use Primary Residence
 - **“Complete Destruction”**
 - **“Unforeseen Circumstances”**
 - **“Modified” General Rules**
- Must have been your personal residence 2 out of the last 5 years (pro-rata exclusion amount if less than 2 years)

How do I find copies of prior tax returns?

- Start with your CPA, bookkeeper or online filing service as they should have records to provide (Turbo Tax, Tax Act, etc.)
- Submit Form 4506 to obtain copies directly from the IRS. The fees are typically waived for counties located in the “**Federal Disaster Declaration**” (DR) zone. Simply write, in red at the top of the Form 4506, the official disaster title
- The IRS has information for taxpayers in reconstructing records after a disaster. Go online to:
 - [https://www.irs.gov/newsroom/reconstructing-records-after-a-disaster-irs-provides-tips-to-help-taxpayers.](https://www.irs.gov/newsroom/reconstructing-records-after-a-disaster-irs-provides-tips-to-help-taxpayers)

Do I want/need professional help?

- It is possible to offset tax on insurance recovery proceeds by replacing the home/contents and or using an IRS exclusion allowance
- Time limits and allowances established by the IRS are extremely important to track to protect your resources
- Failing to report a casualty event on a tax return could result in an audit and or penalties
- It is difficult to calculate and successfully claim a “**Casualty Loss**” for tax purposes
- Changing rules and complexity often make it wise to seek advice from a qualified, vetted expert
- <https://uphelp.org/recovery/professional-help-directory/>
- <https://uphelp.org/claim-guidance-publications/hiring-professional-help-for-an-insurance-claim/>

Stay Informed – Sign UP

To be added to our mailing list for notices of future events and updated guidance:

- Encourage friends to sign up:
www.uphelp.org/signup
- To request a copy of today's slides or video,
email: info@uphelp.org

Stay Connected to Other Disaster Survivors – S2S Forums

- Great Source of Information About:
 - Insurance and Rebuilding
 - Negotiation and Financial Strategies
 - Referrals and Warnings re: professionals
 - Important Source of Emotional Support
 - No one else understands your challenges and emotions like another survivor
- Find upcoming Survivor 2 Survivor Forums and register at: <http://www.uphelp.org/events>

Upcoming Roadmap to Recovery™ Events

www.uphelp.org/events

UPCOMING EVENTS

- Taxes and Financial Decision-making After a Wildfire Loss – a Q&A webinar**
Thursday, March 25, 2021
1:30 PM PT
Zoom - registration required
2020 California wildfire survivors
- Pro Bono Insurance Legal Help Clinic**
Wednesday, March 31, 2021
2:00pm - 5:00pm PT
Zoom
2020 Oregon Wildfire Survivors
- Survivor to Survivor Forum**
Tuesday, April 6, 2021
7:00 PM PT / 8:00 PM MT
Zoom - registration required
All Wildfire Survivors
- Roadmap to Recovery Q&A**
Wednesday, April 7, 2021
5:30pm
Zoom - registration required
2018/2019 California wildfire survivors
- Options and Decision Points for Replacing Your Dwelling**
Thursday, April 8, 2021
4:00 p.m. PT
Zoom - registration required
2020 California wildfire survivors
- Restoring a Wildfire-damaged Standing Home**
Wednesday, April 14, 2021
4:30PM PT / 5:30PM MT
Zoom - registration required
2020 Colorado wildfire survivors and 2020 Oregon wildfire survivors

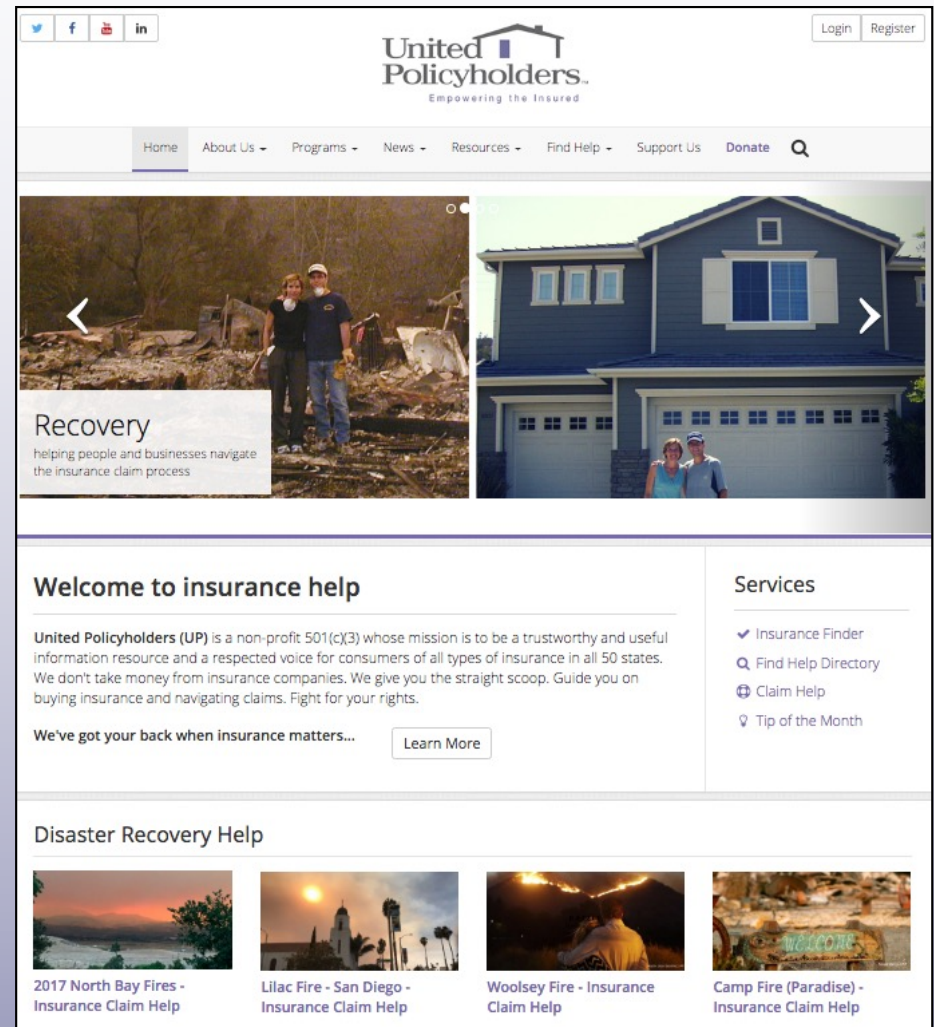
Register for upcoming events.
View recordings of past events and related resources.

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Thank you!

www.uphelp.org/signup

- To be added to our mailing list for notices of future events and updated guidance



The screenshot shows the homepage of United Policyholders. At the top, there are social media icons for Twitter, Facebook, YouTube, and LinkedIn, along with 'Login' and 'Register' buttons. The main header features the United Policyholders logo with the tagline 'Empowering the Insured'. Below the header is a navigation menu with links for Home, About Us, Programs, News, Resources, Find Help, Support Us, and Donate. The main content area is divided into two columns. The left column features a 'Recovery' section with a photo of a couple standing in front of a destroyed house and the text 'Recovery helping people and businesses navigate the insurance claim process'. The right column features a photo of a couple standing in front of a new blue house. Below these columns is a 'Welcome to insurance help' section with a 'Learn More' button. To the right of this section is a 'Services' sidebar with links for Insurance Finder, Find Help Directory, Claim Help, and Tip of the Month. At the bottom, there is a 'Disaster Recovery Help' section with four featured articles: '2017 North Bay Fires - Insurance Claim Help', 'Lilac Fire - San Diego - Insurance Claim Help', 'Woolsey Fire - Insurance Claim Help', and 'Camp Fire (Paradise) - Insurance Claim Help'.

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Center for Disaster Philanthropy



Please complete our short survey
www.uphelp.org/surveyCA

2020 California Wildfires
6 Month – Insurance and Recovery Survey

Purpose: Track insurance and recovery progress and problems. You may take the survey anonymously. The data collected helps us serve your community and informs our advocacy work.

Thank you!