

2020
National Income Tax Workbook
Chapter 9: Individual Issues – PART 1

Learning Objectives

pg 293

Understand

Understand what health, in-home care, and long-term care expenses qualify for as a medical deduction

Know

Know the COVID-19 relief that applies to health savings accounts, cafeteria plans, and flexible spending arrangements

Understand

Understand when a taxpayer can claim personal casualty loss or a business casualty loss

Calculate
and report

Calculate and report the amount of a casualty loss or gain

Know

Know the tax rules that apply to disaster relief payments

Issue 2: Casualty

Losses

Pg. 302

Casualty Defined



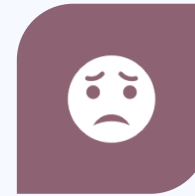
FEDERALLY DECLARED
DISASTER – WEATHER
OR ECONOMIC



SUDDEN, UNEXPECTED,
UNUSUAL, SWIFT



CAUSES DAMAGE OR
DESTRUCTION



UNEXPECTED,
UNINTENDED,
UNUSUAL EVENT



DESTRUCTION OF
PROPERTY – NOT
CAUSED BY PETS,
WILLFUL ACTS OR
WILLFUL NEGLIGENCE

Casualty Loss NOT in Book

- **Michigan federally declared disaster in 2020**
- **Flooding & Severe Storms**

EM-3525-MI Midland & Gladwin

DR-4547 Midland, Gladwin, Arenac, Iosco, Saginaw

Michigan Disasters 2020

- [Michigan SEVERE STORMS AND FLOODING \(DR-4547-MI\)](#)
 - Incident Period: May 16, 2020 - May 22, 2020 Major Disaster Declaration declared on July 9, 2020
- [Michigan SEVERE STORMS AND FLOODING \(EM-3525-MI\)](#)
 - Incident Period: May 16, 2020 and continuing Emergency Declaration declared on May 21, 2020
- [Michigan COVID-19 PANDEMIC \(DR-4494-MI\)](#)
 - Incident Period: January 20, 2020 and continuing
 - Major Disaster Declaration declared on March 27, 2020
- [Michigan COVID-19 \(EM-3455-MI\)](#)
 - Incident Period: January 20, 2020 and continuing
 - Emergency Declaration declared on March 13, 2020

Personal Property

pg 302 - 303

- I.R.C. § 165(c)(3) – losses allowable if casualty
 - 2018 thru 2025 = Federally Declared Disaster Areas only
- Calculating a loss = smaller of
 - Property's adjusted tax basis
 - Decreased in FMV
- Reduce gross loss by insurance proceeds
 - Proceeds > deductible loss = NO LOSS
 - Reportable Gain?

Loss Deduction Limits

pg 303

- \$100 for each separate casualty
- 10% of taxpayer's AGI (after \$ 100 reduction) = SUM of all personal casualty losses
- Practitioner Note: Disaster Relief Act of 2019
 - Continued until 1/19/20 & declared before 2.19.20
 - \$500 for each separate casualty & NO 10% AGI limitation even if don't itemize
 - Occurred in 2018 AND before Dec 21, 2019

Losses Offset Gains

pg 303



Examples

pg 303

Example 9.5 Personal Casualty Loss

- ✓ \$ 10,000 personal casualty loss
- ✓ \$ 85,000 AGI
- ✓ NO deductible loss (no federal disaster)

Example 9.6 Personal Casualty Loss Offset

- ✓ \$ 16,000 personal casualty gain
- ✓ \$ 10,000 personal casualty loss
- ✓ \$ 85,000 AGI
- ✓ \$ 6,100 casualty gain ($\$ 16,000 - (10,000 - 100)$)

Example 9.7 Federally Declared Disaster Loss

pg 303

- ✓ Same facts as 9.6 except
- ✓ \$ 20,000 personal casualty loss
- ✓ Federally declared disaster
- ✓ \$ 6,100 loss offsets \$ 6,100 gain
- ✓ \$ 5,300 deductible loss $[(\$ 20,000 - 100) - \$ 6,100 \text{ gain} - \$ 8,500 \text{ AGI limit}]$

Costs Not Included in Loss

pg 303 -304

- Cleaning after casualty
- Repairing or replacing damaged/destroyed property
- Temporary housing
- Rental car
- Incidental expenses
- Decreased FMV = substantiation

PRACTITIONER NOTE

Protective Measures

The taxpayer cannot include in a casualty loss deduction the cost of proactive measures taken to protect personal property from a potential casualty loss. Such measures include boarding up windows in anticipation of a hurricane and sand-bagging an area in anticipation of a flood. The taxpayer can deduct the cost to protect business property as a business expense.

Proof of Loss

pg 304

- Type of casualty and when it occurred
- And direct result of the casualty
- That taxpayer owed the property (or, if the taxpayer leased the property, that the taxpayer was contractually liable to the owner for the damage)
- Whether there is a reasonable expectation of recover from a claim for reimbursement



Calculating a Gain

pg 304

- Involuntary conversion rules
 - Reinvest in similar or related use property
 - Replacement period
 - 2 years after year of gain
 - 4 years after year of loss
- Treas. Reg. § 1.1033(a)-2(b) – nonrecognition of gain is mandatory if property is involuntarily or compulsorily converted

Example 9.8

pg 304 - 305

- 2020 Hurricane destroyed garage
- Basis \$ 15,000
- Insurance proceeds \$ 35,000
- Rebuild costs \$ 45,000
- Deferred Gain = \$ 20,000 (35,000 – 15,000)

FIGURE 9.2 Statement re Deferral of Casualty Gain

Deferral of Casualty Gain under I.R.C. § 1033	
On February 8, 2020, Jenna Silverstein realized a casualty gain from the collapse of a garage caused by a hurricane. The taxpayer postpones this casualty gain and has purchased replacement property that is similar or related in use.	
Insurance proceeds received	\$35,000
Adjusted tax basis	(15,000)
Gain realized	\$20,000
Gain deferred	(20,000)
Gain recognized	\$ 0
Cost of replacement property (garage)	\$45,000
Gain deferred	(20,000)
Basis of replacement property	\$25,000

Reporting Individual Losses & Gains pg 305

- Form 4684, Section A
- I.R.C. § 165 = ordinary
- Form 1040, Schedule A if loss
- Form 1040, Schedule D if gain

Example 9.9 Casualty Loss

pg 305

- 2020 Tornado
- Federally declared disaster area
- Personal residence and personal property destroyed
- Coin collection
- Gain from insurance proceeds

FIGURE 9.3 Tornado Damaged Personal Property

Item	Date Acquired	Adjusted Basis	FMV Before	FMV After	Difference In FMV	Insurance Payment	Gain or (Loss)
House, land, and trees	2/01/2007	\$287,000	\$523,000	\$235,000	\$288,000	\$257,000	\$ (30,000) ¹
Household items	Various	86,878	65,000	0	65,000	50,000	(15,000) ²
Coin collection	Various	3,546	6,000	0	6,000	6,000	2,454 ³
Anne's car	7/19/2018	14,000	13,000	0	13,000	0	(13,000) ⁴

¹ \$257,000 insurance proceeds – \$287,000 adjusted basis (\$287,000 cost basis is less than the \$288,000 reduction in FMV)

² \$50,000 insurance proceeds – \$65,000 decrease in FMV (\$65,000 decrease in FMV is less than the \$86,878 adjusted basis)

³ \$6,000 insurance proceeds – \$3,546 adjusted basis (\$3,546 adjusted basis is less than the \$6,000 decrease in FMV)

⁴ \$0 insurance proceeds – \$13,000 decrease in FMV (\$13,000 decrease in FMV is less than the \$14,000 adjusted basis)

FIGURE 9.4 Form 4684, Casualties and Thefts, Section A, Personal Use Property

<p>Form 4684</p> <p>Department of the Treasury Internal Revenue Service</p> <p>Name(s) shown on tax return Charles and Marie Seidel</p>	<p>Casualties and Thefts</p> <p>► Go to www.irs.gov/Form4684 for instructions and the latest information. ► Attach to your tax return. ► Use a separate Form 4684 for each casualty or theft.</p>	<p>OMB No. 1545-0177</p> <p>2019</p> <p>Attachment Sequence No. 26</p> <p>Identifying number XXX-XX-XXXX</p>
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SECTION A—Personal Use Property (Use this section to report casualties and thefts of property **not** used in a trade or business or for income-producing purposes. You must use a separate Form 4684 (through line 12) for each casualty or theft event involving personal use property. **If reporting a qualified disaster loss, see the instructions for special rules that apply before completing this section.**)

If the casualty or theft loss is attributable to a federally declared disaster, check here ☒ and enter the FEMA disaster declaration number. (See instructions.) DR-4478

Description of properties (show type, location city, state, and ZIP code), and date acquired for each property. Use a separate line for each property lost or damaged from the same casualty or theft. If you checked the box and entered the FEMA disaster declaration number above, enter the ZIP code for the property most affected on the line for Property A.	Type of Property	City and State	ZIP Code	Date Acquired
Property A	PERSONAL RESIDENCE	SLEEPY ROCK, MISSISSIPPI	38618	02/01/2007
Property B	PERSONAL HOUSEHOLD ITEMS	SLEEPY ROCK, MISSISSIPPI	38618	VARIOUS
Property C	COIN COLLECTION	SLEEPY ROCK, MISSISSIPPI	38618	VARIOUS
Property D				

	A	B	C	D
2 Cost or other basis of each property	287,000	86,878	3,548	
3 Insurance or other reimbursement (whether or not you filed a claim) (see instructions). Note: If line 2 is more than line 3, skip line 4.	257,000	50,000	6,000	
4 Gain from casualty or theft. If line 3 is more than line 2, enter the difference here and skip lines 5 through 8 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.			2,454	
5 Fair market value before casualty or theft	523,000	65,000		
6 Fair market value after casualty or theft	235,000	0		
7 Subtract line 6 from line 5	288,000	65,000		
8 Enter the smaller of line 2 or line 7	287,000	65,000		
9 Subtract line 3 from line 8. If zero or less, enter -0-	30,000	15,000		
10 Casualty or theft loss. Add the amounts on line 9 in columns A through D				45,000
11 Enter \$100 (\$500 if qualified disaster loss rules apply; see instructions)				100
12 Subtract line 11 from line 10. If zero or less, enter -0-				44,900
Caution: Use only one Form 4684 for lines 13 through 15.				
13 Add the amounts on line 4 of all Forms 4684				2,454
14 Add the amounts on line 12 of all Forms 4684. If you have losses not attributable to a federally declared disaster, see the instructions. Caution: See instructions before completing line 15.				44,900
15 • If line 13 is more than line 14, enter the difference here and on Schedule D. Do not complete the rest of this section. • If line 13 is equal to line 14, enter -0- here. Do not complete the rest of this section. • If line 13 is less than line 14, and you have no qualified disaster losses subject to the \$500 reduction on line 11 on any Form(s) 4684, enter -0- here and go to line 16. If you have qualified disaster losses subject to the \$500 reduction, subtract line 13 from line 14 and enter the smaller of the difference or the amount on line 12 of the Form(s) 4684 reporting those losses. Enter that result here and on Schedule A (Form 1040 or 1040-SR), line 16, or Form 1040-NR, Schedule A, line 7. If you claim the standard deduction, also include on Schedule A (Form 1040 or 1040-SR), line 16, the amount of your standard deduction (see the instructions for Forms 1040 and 1040-SR). Do not complete the rest of this section if all of your casualty or theft losses are subject to the \$500 reduction.				0
16 Add lines 12 and 15. Subtract the result from line 14				42,446
17 Enter 10% of your adjusted gross income from Form 1040 or 1040-SR, line 8b, or Form 1040-NR, line 35. Estates and trusts, see instructions				15,800
18 Subtract line 17 from line 16. If zero or less, enter -0-. Also, enter the result on Schedule A (Form 1040 or 1040-SR), line 15, or Form 1040-NR, Schedule A, line 6. Estates and trusts, enter the result on the "Other deductions" line of YOUR tax return				26,646

For Paperwork Reduction Act Notice, see instructions. Cat. No. 1 (9970) **Form 4684** (2019)

Topics on pg 308

- Multiple Casualties during the year
- Mixed-Use Property
- Timing & Deductibility of Losses
- Reimbursement $<$ expected = Loss
- Reimbursement $>$ expected = Additional Income

Temporary Living Expenses

pg 308

- I.R.C. § 123 – insurance reimbursement excluded from income
- Costs = actual temporary living expenses - household's normal expenses
- Expenses = rent, meals, utilities, transportation, laundry, misc
- Excess payments = taxable income

Example 9.10
Reimbursed
Temp. Living
Exp

Facts same as 9.9

Insurance proceeds for Temp Living = \$ 15,900

Normal living costs = \$ 10,000

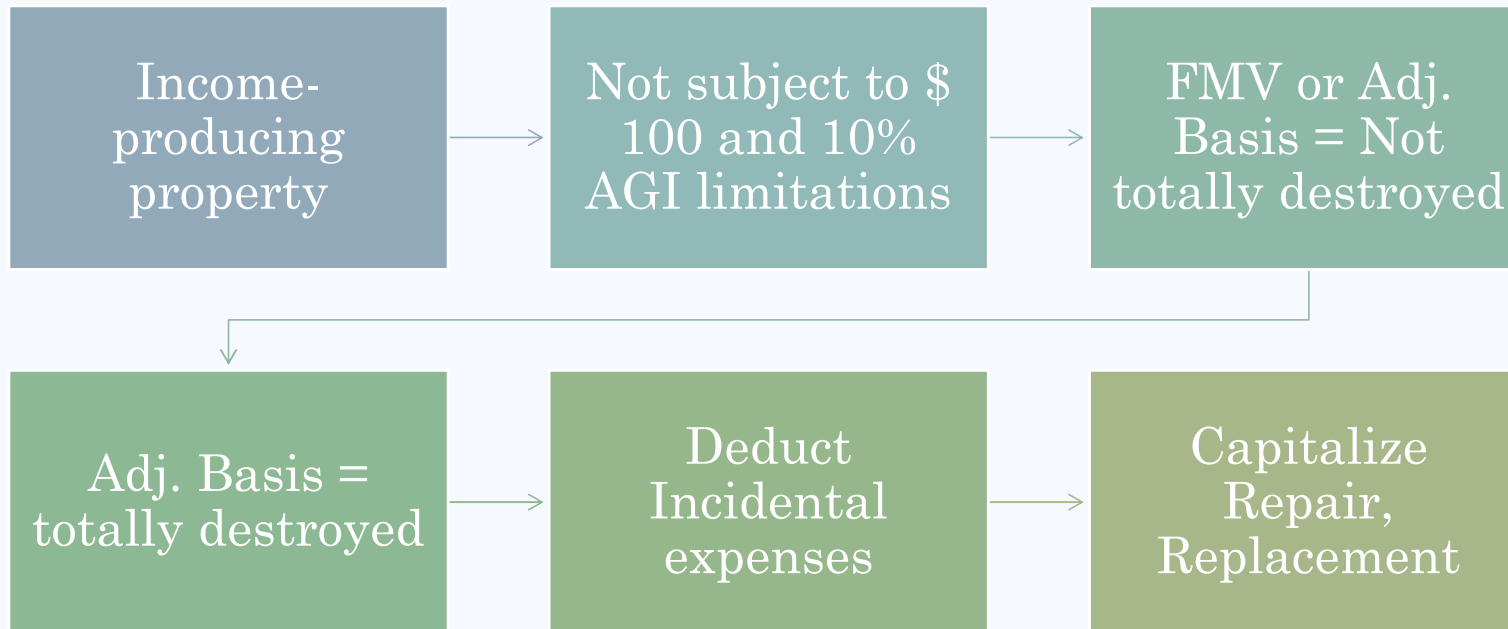
Actual Temp Living costs = \$ 14,500

Exclude \$ 4,500 ($14,500 - 10,000$)

Taxable Income = \$ 11,400 ($15,900 - 4,500$)

Business Property

pg 309



Deduction of Loss

pg 309



Form 4684,
Section B



Investment – Form
1040, Schedule A



Business Property –
form 4797

PRACTITIONER NOTE

Passive Activity Loss Limits

Treas. Reg. § 1.469-2(d)(2)(xi) excepts casualty losses from the passive activity loss deduction limits.

PRACTITIONER NOTE

Casualty Gain

Prior use of the section 179 expense election and accelerated depreciation frequently results in a casualty gain. However, the taxpayer may be able to defer that gain if he or she purchases replacement property. The deferral of gain is discussed later in this section.

Example 9.11
Trade or Business
Prop. Loss

pg 309

- 2015 Purchased Business Building
= \$ 245,000
- Adj. Basis = \$ 225,000
- 2020 tornado destroyed building
- Insurance proceeds = \$ 155,000
- Loss = \$ 57,377 ($212,377 - 155,000$)
- Form 4684, Schedule B

FIGURE 9.5 Form 4684, Casualties and Thefts
Section B, Business and Income-Producing Property

Name(s) shown on tax return. Do not enter name and identifying number if shown on other side. Charles and Marie Seidel		Identifying number 999-99-9999	
SECTION B—Business and Income-Producing Property			
Part I Casualty or Theft Gain or Loss (Use a separate Part I for each casualty or theft.)			
10 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft. See instructions if claiming a loss due to a Ponzi-type investment scheme and Section C is not completed.			
Property A WAREHOUSE BUILDING, SILBERT ROCK, MD, 2/10/2012			
Property B			
Property C			
Property D			

	Properties			
	A	B	C	D
20 Cost or adjusted basis of each property	212,377			
21 Insurance or other reimbursement (whether or not you filed a claim). See the instructions for line 3. Note: If line 20 is more than line 21, skip line 22.	155,000			
22 Gain from casualty or theft. If line 21 is more than line 20, enter the difference here and on line 29 or line 34, column (c), except as provided in the instructions for line 33. Also, skip lines 23 through 27 for that column. See the instructions for line 4 if line 21 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year.				
23 Fair market value before casualty or theft	225,000			
24 Fair market value after casualty or theft	0			
25 Subtract line 24 from line 23	225,000			
26 Enter the smaller of line 20 or line 25. Note: If the property was totally destroyed by casualty or lost from theft, enter on line 26 the amount from line 20.	212,377			
27 Subtract line 21 from line 26. If zero or less, enter -0-	57,377			
28 Casualty or theft loss. Add the amounts on line 27. Enter the total here and on line 29 or line 34 (see instructions)				57,377

Part II Summary of Gains and Losses (from separate Parts I)		(b) Losses from casualties or thefts		(d) Gains from casualties or thefts includable in income	
(a) Identify casualty or theft		(i) Trade, business, rental, or royalty property	(ii) Income-producing property		
Casualty or Theft of Property Held One Year or Less					
29		0	0		
30 Total. Add the amounts on line 29	0	0	0		
31 Combine line 30, columns (bi) and (ci). Enter the net gain or (loss) here and on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions				0	
32 Enter the amount from line 30, column (bi) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040 or 1040-SF), line 16, or Form 1040-NR, Schedule A, line 7. (Do not include any loss on property used as an employee.) Estates and trusts, partnerships, and S corporations, see instructions					0
Casualty or Theft of Property Held More Than One Year					
33 Casualty or theft gains from Form 4797, line 32					0
34 TORNADOES		57,377	0		
35 Total losses. Add amounts on line 34, columns (bi) and (ci)	57,377	57,377	0		
36 Total gains. Add lines 33 and 34, column (ci)				0	
37 Add amounts on line 35, columns (bi) and (ci)					-57,377
38 If the loss on line 37 is more than the gain on line 36:					
a. Compare line 35, column (bi) and line 36, and enter the net gain or (loss) here. Partnerships and S corporations, see the Note below. All others, enter this amount on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions				-57,377	
b. Enter the amount from line 35, column (bi) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040 or 1040-SF), line 16, or Form 1040-NR, Schedule A, line 7. (Do not include any loss on property used as an employee.) Estates and trusts, enter on the "Other deductions" line of your tax return. Partnerships and S corporations, see the Note below					-57,377
39 If the loss on line 37 is less than or equal to the gain on line 36, combine lines 36 and 37 and enter here. Partnerships, see the Note below. All others, enter this amount on Form 4797, line 3					-57,377
Note: Partnerships, enter the amount from line 38a, 38b, or 39 on Form 1065, Schedule K, line 11. S corporations, enter the amount from line 38a or 38b on Form 1120-S, Schedule K, line 10.					

Example
9.12
Rental
Property
Loss
pg 311

- Rental Home purchased \$ 185,000
- Adj. Basis \$ 121,379
- FMV \$ 245,000
- 2020 Wildfire, no insurance
- Estimated Restoration cost \$ 75,350
- Loss Deduction \$ 75,350 (lower of Adj. Basis or restoration cost)
- Adjust Basis by Loss Deduction

Example 9.13

Income- Producing Property Loss

pg 311

Gem investor

Lockbox in basement for his Gems

Basis \$ 7,855

Uninsured

2020 basement flooded and Gems lost

Loss Deduction \$ 7,855

Form 1040, Schedule A

FIGURE 9.6 Dori Frank's Schedule A (Form 1040), Itemized Deductions

Casualty and Theft Losses	15	Casualty and theft losses from a federally declared disaster (other than net qualified disaster losses). Attach Form 4684 and enter the amount from line 18 of that form. See instructions	15	26,647
Other Itemized Deductions	16	Other—from list in instructions. List type and amount ▶ _____		
		FORM 4684, INCOME PRODUCING PROPERTY 7,855	16	7,855

OBSERVATION

Income-Producing Property Losses

Losses on income producing property are miscellaneous itemized deductions that are not subject to the 2%-of-AGI reduction. Income producing property for this purpose is property held for investment. Because the IRS considers rental real estate to be business property for a casualty loss deduction, taxpayers can deduct a rental property loss even if they did not itemize deductions.

Deferral of Gain

pg 312



Reimbursement =
similar property



Basis in new property
= Adj. of replaced
property



Realizes & Reports
Gain = money or
unlike property
received



Deferred Gain =
similar property



Postponed Gain – only
if cost of replacement
= reimbursement
amount



Excess
Reimbursement =
included income

Replacement Period

Pg 312

- 2 years after close of 1st tax year of realized gain
- 4 years following loss of main home in Federally Declared Disaster Area
- Extension of replacement period – apply to IRS
 - Limited to not more than 1 year
 - Construction of replacement period – IRS may grant extension

Replacement Property pg 312

- Specified use, purpose & similar
- Cannot be gifted or inherited
- Can use borrowed funds
- Federally declared disaster area

- Purchased Truck \$ 46,500
- Business Use
- Elected § 179
- Adj. Basis = \$ 0
- 2020 Mudslide
- Federally declared disaster area
- Insurance Proceeds \$ 32,000
- Gain = \$ 32,000 (Insurance Proceeds – Adj. Basis)
- Ordinary Gain - § 1245 Recapture
- Form 4797, Part III

Example 9.14

Basis of Replacement Property pg 313

FIGURE 9.7 Samantha Saunders's Form 4797, Part III

Form 4797 (2018)

Page **2**

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255
(see instructions)

19	(a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
	A 2019 FORD F350	2/01/2019	2/10/2020
	B		
	C		
	D		

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20	Gross sales price (Note: See line 1 before completing.)	20	32,000		
21	Cost or other basis plus expense of sale	21	46,500		
22	Depreciation (or depletion) allowed or allowable	22	46,500		
23	Adjusted basis. Subtract line 22 from line 21.	23	0		
24	Total gain. Subtract line 23 from line 20.	24	32,000		
25	If section 1245 property:				
a	Depreciation allowed or allowable from line 22	25a	46,500		
b	Enter the smaller of line 24 or 25a	25b	32,000		
26	If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.				
a	Additional depreciation after 1975. See instructions.	26a			
b	Applicable percentage multiplied by the smaller of line 24 or line 26a. See instructions.	26b			
c	Subtract line 26a from line 24. If residential rental property or line 24 isn't more than line 26a, skip lines 26d and 26e	26c			
d	Additional depreciation after 1969 and before 1976.	26d			
e	Enter the smaller of line 26c or 26d	26e			
f	Section 291 amount (corporations only)	26f			
g	Add lines 26b, 26e, and 26f	26g			
27	If section 1252 property: Skip this section if you didn't dispose of farmland or if this form is being completed for a partnership.				
a	Soil, water, and land clearing expenses	27a			
b	Line 27a multiplied by applicable percentage. See instructions.	27b			
c	Enter the smaller of line 24 or 27b	27c			
28	If section 1254 property:				
a	Intangible drilling and development costs, expenditures for development of mines and other natural deposits, mining exploration costs, and depletion. See instructions.	28a			
b	Enter the smaller of line 24 or 28a.	28b			
29	If section 1255 property:				
a	Applicable percentage of payments excluded from income under section 126. See instructions.	29a			
b	Enter the smaller of line 24 or 29a. See instructions.	29b			

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30	Total gains for all properties. Add property columns A through D, line 24	30	32,000
31	Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	32,000
32	Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	0

- Same facts as 9.14
- Replaces truck by 2020
 - Any tangible business property
 - Postponed gain
- Adj. Basis of replacement property = purchase price – insurance proceeds
 - New truck \$ 48,000
 - Adj. Basis = \$ 16,000 (\$ 48,000 – 32,000)
- If NOT Federally declared disaster area – replacement property = similar property

Example 9.15
pg 315

Loss of Inventory pg 315

Reporting Method 1:

- Record loss as increased COGS
- Gross Income = insurance proceeds, sales, reimbursements
- Cannot claim Casualty Loss

Reporting Method 2:

- Deduct loss separately
- Form 4684
- Removes from COGS
- Form 4684 = Reimbursements received

Example 9.16

pg 315

- Business in Federally declared disaster area
- Kitchen cabinets = \$ 38,000
- Storm damage = \$ 6,500
- Labor & Material cost = \$ 6,500
- Sold cabinets for \$ 18,000
- Net loss = \$ 26,500 ($\$ 18,000 - \$ 38,000 - \$ 6,500$)
- Report on Form 1040, Schedule C
 - COGS = \$ 44,500 ($\$ 38,000 + \$ 6,500$)
 - Income = \$ 18,000
- OR Report on Form 4684, Section B
 - Nothing on Schedule C
- Practitioner Note: Timing Differences

Issue 3: Disaster Relief

- Federal Emergency Management Agency (FEMA) – administers relief
- 2020 Nationwide Emergency -- § 501(b)
 - Due to COVID-19

Robert T. Stafford
Disaster Relief &
Emergency
Assistance Act
(Act 42 U.S.C.
Chapter 68)

Disaster Relief Payments

pg 317

Grants

Loan
Cancellation

Qualified
Disaster
Relief

Qualified
Disaster
Mitigation

Stimulus
Payment

Practitioner Note – Relief Programs

Small Business Administration Programs

Paycheck Protection (PPP) Chap. 16

Economic Disaster Relief Loans (EIDL)

EIDL Advance

- Under Disaster Relief Act –
NO COD on forgiveness
 - Reimbursement for the loss
 - Reduces casualty loss deduction

Federal Loan
Canceled
pg 316

- Not included in income
- Eligible expense
 - Reasonable and necessary personal, family, living, or funeral expenses incurred as a result of the qualified disaster
 - Reasonable and necessary expenses for repair or rehabilitation of a personal residence (rented or owned) to the extent the need for repair or rehabilitation is attributable to the qualified disaster
 - Reasonable and necessary expenses for repair or replacement of the contents of a personal residence to the extent the need for repair or replacement is attributable to the qualified disaster
- Payments to promote the general welfare by federal, state or local governments
- Practitioner Note: COVID-19 Employer Relief

Qualified Disaster Relief Payments

Qualified Disaster Mitigation Payments

Excludable from income
AND no basis adjustment

Does not apply to amounts
from sale or disposition

- 2020 FEMA Grant to elevate the house
- Form 1099 received – “other income”
- Excludable income
- No basis Adj. of the home

Example 9.17 Flood Hazard Mitigation

Practitioner
Note —
Grants
to
Business
pg 317

- NOT excludable
- I.R.C. § 139 – applies only to individuals
 - not for general welfare
- I.R.C. § 1033 – elect to defer gain realized

Principal Residence in a Disaster Area – Gain Recognition

pg 318

No recognized gain – unscheduled
personal property

Single item of property, similar or related
in use

Replacement period 4 years after end of
year gain realized

- Principal residence
- 2020 flood – federally declared disaster
- Insurance proceeds = \$ 200,000
- Unscheduled personal property proceeds = \$ 25,000
- Scheduled personal property proceeds = \$ 5,000 Jewelry & \$ 10,000 stamp collection
- No gain on unscheduled personal property
- Postponed gain \$ 215,000

Example 9.18 Insurance Gain in Disaster Area

pg 318

- 1 year for most affected by federally declared disaster area
- Abatement of interest & penalties
- If qualify write reason in margin of tax return, ex. “Texas Tornadoes”
- Affected Taxpayers:
 - Main home in covered disaster area
 - Business entity or sole proprietorship principal place of business in covered disaster area
 - Relief worker assisting victims in covered disaster area
 - Individual, business entity or sole proprietorship whose records were in covered disaster area
 - Estate or trust whose records were in covered disaster area
 - Spouse on a joint return with a taxpayer who is eligible for postponements
 - Any other person who the IRS determines to be affected

Postponed Tax Deadlines pg 318

COVID-19 Postponements

pg 319

- July 15th
- Rev. Proc. 2018-58,
2018-50
- I.R.B. 990
- Notice 2020-23



PRACTITIONER NOTE

State Income Tax

This relief applies only to certain federal tax filing and payment deadlines. State filing and payment deadlines vary and are not always the same as the federal filing and payment deadline. Thus, the tax practitioner should check with his or her state tax agencies for information about deadlines.

CROSS-REFERENCE

Employment Taxes

See the "New Legislation: Part 2" chapter in this book for discussion of relief that allows employers to delay the deposit of certain employment taxes.

Timing of Loss Deduction

pg 319



YEAR OF LOSS



PRECEDING YEAR



ELECT PRIOR YEAR – 6
MONTH AFTER DUE
DATE

Polling Question 1

A Federally Declared Disaster Area may be due to:

- a. Tornado
- b. Flood
- c. Economic
- d. All of the above

Issue 1: Health Care Deduction

Medical & Dental Expense

pg 294

- Itemized deduction subject to 7.5% of AGI
 - January 01, 2019 thru December 31, 2020
- Health Savings Account (HSA) Contributions
- Flexible Spending Arrangements (FSA) Contributions
- Health Reimbursement Arrangement (HRA)

Example 9.1 Calculating the Deduction

- Henry & Wanda are married with one dependent child
- AGI = \$ 300,000
- Medical Expenses of \$ 30,000
- \$ 5,000 Insurance Reimbursement

How much is their eligible medical expenses if they itemize?

- \$ 25,000

How much is their allowable medical deduction if they itemize?

- \$ 2,500 ($\$ 25,000 - 300,000 \times 7.5\%$)



Definition of Medical Care

1. for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body;
2. for transportation primarily for and essential to medical care described in (1):



Definition of Medical Care

3. For qualified long-term care services [as defined in I.R.C. § 7702B(c) and discussed later]: OR
4. For insurance (including amounts paid as Medicare Part B premiums) covering medical care described in (1) or (2), or for any qualified long-term care insurance contract [as defined in I.R.C. § 7702B(b) and discussed later].



Other eligible medical expenses pg 295

- Lodging
 - Away from home for essential medical care
 - Medical care provided by physician in licensed hospital (or equivalent)
 - No significant element of personal pleasure
 - \$ 50 per night per person maximum
- Prescribed Drugs
 - Prescribed by physician
 - Drug or biological used by an individual
 - I.R.C. § 216(b)
 - Not Controlled substances like Marijuana

NOT IN THE CHAPTER

Practitioner Pointer

Medical Marijuana

- Rev. Rul. 97-9. 1997-1CB77 – controlled substances are ineligible prescription drug
- Treas. Reg § 1.213-1(e)(2) – prescription must be legally procured
- Pub 502 – illegal/controlled substances are ineligible
- INFO 2010-0080 Chief Counsel Letter to Senator Schumer
 - Naturopathic care, including herbs, can qualify as medical care
 - Dickie v. Commissioner, T.C. Memo. 1999-138
 - Crain v Commissioner, T.C. Memo. 1986-138
 - Tso v Commissioner, T.C. Memo 1980-399

Capital Expenditures

pg 295

- Eye glasses
- Seeing eye dog
- Artificial teeth & limbs
- Durable medical equipment – wheelchair, crutches, inclinor or air conditioner detachable from property
- Permanent improvement or betterment of property
> increased value of the related property

Example 9.2 – Improvement to Property

- Cindy has heart disease
- Physician advises her to install an elevator
- Cost of elevator = \$ 20,000
- Increased value of residence = \$ 10,000
- Eligible medical expense = \$ 10,000 ($\$ 20,000 - 10,000$)
- Cost of installation separate from cost of elevator = 100% medical expense because it does not increase the value of the residence

Polling Question 2



Individual taxpayers who itemize deductions can deduct medical expenses that exceed:

- a. 10% of AGI
- b. 12% of AGI
- c. 7.5% of AGI
- d. 5.5% of AGI

Long-Term Care

pg 295

§ 213(d) –
define medical
services

Medically
necessary
diagnostic

Preventive

Therapeutic

Curing

Treating

Mitigating

Rehabilitative
services

Maintenance
or personal
care services

Chronically Ill Individual

pg 295

- Is unable to perform (without substantial assistance from another individual) at least 2 ADL's (eating, bathing, or dressing) for a period of at least 90 days due to a loss of functional capacity;
- Has a level of disability similar to the level of disability described in (1); OR
- Requires substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment

Institution
Expenses
pg 295-296

Treas. Reg. § 1.213-
1(e)(1)(v)

Inpatient hospital care

Non-hospital Care –
Facts & Circumstances

Example 9.3 Meals & Lodging

pg 296

Patricia, 80 years old

```
graph TD; A[Patricia, 80 years old] --> B[Moved to nursing home]; B --> C[Medication management only]; C --> D[Meals & lodging are NOT medical care];
```

Moved to nursing home

Medication management only

Meals & lodging are NOT medical care

Baker v. Commissioner, 122 T.C. 143

- Independent living facility
- Percentage method to total monthly service fees
 - Allocable to medical care

Education Expenses

pg 296

- Special school for special needs individual
- Cost include:
 - Meals & lodging
 - Ordinary education
 - Medical care – cost of care and supervision, or of treatment & training, of a mentally or physically handicapped person at a school etc.

At-Home Care Expenses

pg 296-297

- I.R.C. § 262 – disallows a deduction for personal living & family expenses that are not medical
- Estate of Marantz v. Commissioner, 39 T.C.M. 515 (1979)
 - 40% Medical expense for caregivers

PRACTITIONER NOTE

Employment Taxes

In Rev. Rul. 57-489, 1957-2 C.B. 207, the IRS ruled that the FICA tax paid on an expenditure that qualifies as a medical expense is also a deductible medical expense under section 213.

Rev. Rul. 76-106, 1976-1 C.B. 71

- At-home Caregiver
- Pd wages, meals & lodging
- Apportion time between nursing-type services and other
- Portion of wages not attributed to Medical are NOT deductible
- Example 9.4

Qualified Long-Term Care Insurance Contract

I.R.C. § 7702B

1. The only insurance protection provided under the contract is coverage of qualified long-term care services
2. The contract does not pay or reimburse expenses incurred for services or items to the extent that such expenses are reimbursable under title XVIII of Social Security Act or would be so reimbursable but for the application of a deductible or coinsurance amount
3. The contract is guaranteed renewable
4. The contract does not provide for a cash surrender value or other money that can be paid, assigned, or pledged as collateral for a loan, or borrowed, other than certain allowed refunds
5. All refunds of premiums (other than refunds due to death of the insured or a complete surrender or cancellation of the policy), and all policy holder dividends or similar amounts, under the contract are to be applied as a reduction in further premiums or to increase future benefits
6. The contract provides certain consumer protection provisions specified in §7702B(g)

FIGURE 9.1 Maximum Deductible Long-Term Care Premiums

	2018	2019	2020
40 or less	\$420	\$420	\$430
More than 40, less than 51	780	790	810
More than 50, less than 61	1,560	1,580	1,630
More than 60, less than 71	4,160	4,220	\$4,350
More than 70	5,200	5,270	\$5,430
Maximum excludable long-term care per diem	360	370	380

Limitations on Deductible Premiums

Medical & Dental Expenses of Dependent

I.R.C. § 152
– defines
dependent

- Treas. Reg. § 1.151-2 –
income >
\$ 4,300

- Tie-breaker
rules apply

Multiple
Support
Agreements
– designee
for that
year

PLANNING POINTER

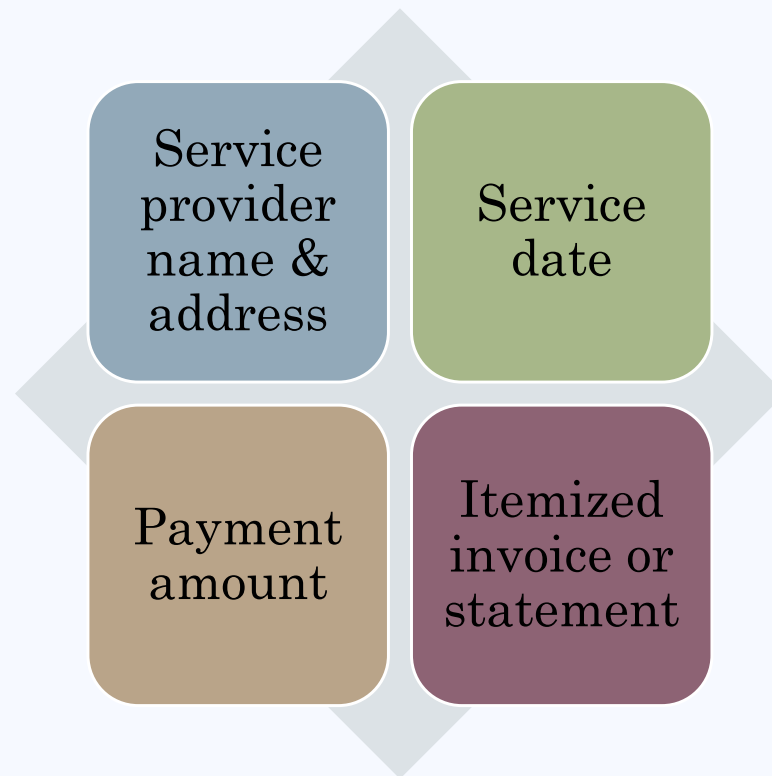
Medical Expense Election

Generally, unpaid medical expenses are not allowed as a deduction on the decedent's individual income tax return but are allowed as a deduction on the estate tax return. With the increased estate tax exemption amount (\$11,580,000 in 2020), most taxpayers no longer have an estate tax liability. In these cases, the executor of the estate can elect to treat any medical expenses paid from the estate within 1 year of the date of death as an itemized deduction [I.R.C. § 213(c)].



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Substantiation of Deductions





Polling Question 3

- There is no limit to the amount of Long-Term Care Premiums a taxpayer may deduct.
 - True or False

Health Savings Account (HSA) pg 299

- Pretax contribution
- Rolls over to next year
- High-deductible Health Plan (HDHP)
- NO Medicare
- Not a Dependent

PLANNING POINTER

Medicare Recipient

Taxpayers enrolled in Medicare cannot contribute to an HSA, but they can use HSA contributions made prior to age 65 to pay the premiums for Medicare Part B, Part D, and Medicare Advantage plans.

HSA Contributions

pg 299

Non-taxable fringe benefit if Employer contributes

- Or Above-the-line deduction

\$ 3,550 self-only coverage

\$ 7,100 family coverage

Over age 55 = \$ 1,000 additional

Distributions from HSA

pg 299



Used exclusively for qualified medical



Non-medical expense =
20% added tax

Exceptions may apply

High-deductible Health Plan

Annual Deductibles

- \$ 1,400 Self-only
- \$ 2,800 Family
- Notice 2019-45, 2019-32 I.R.B. 593 – expands list of preventative care
 - Specified Medical Care Services – treated as preventative care for chronic condition

Flexible Spending Arrangements



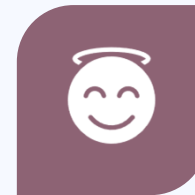
EMPLOYER-
SPONSORED



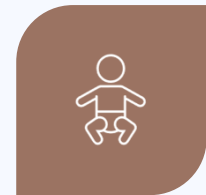
USE IT OR LOOSE
IT



PRE-TAX
CONTRIBUTION



\$ 2,750 MEDICAL



\$ 5,000
DEPENDENT
CARE

CROSS-REFERENCE

Health Reimbursement Arrangements

I.R.C. § 105 allows for the reimbursement of medical expenses under an employer-sponsored health plan. Under an HRA, the employer contributes to the plan. The contributions are excluded from the employee's income. There is no limit on the employer's contribution. Distributions must be paid to reimburse the employee for qualified medical expenses of the employee and his or her spouse and dependents. Unused amounts can be carried over to the next year. See the "Business Tax Issues" chapter in this book for a discussion of HRAs.

PRACTITIONER NOTE

Self-Employed Persons

Self-employed persons are not eligible for an FSA or HRA. For fringe benefit purposes, an S corporation is treated as a partnership, and a 2% shareholder is treated as a partner of the partnership. A 2% shareholder is one that directly or constructively owns more than 2% of the corporation's outstanding stock on any day during the S corporation's tax year. Therefore, greater-than-2% shareholders of S corporations receiving W-2 wages are ineligible to participate in an FSA or HRA.

COVID-19
Plan
Relief
pg 300

- Telehealth: Notice 2020-29 & 2020-22, I.R.B. 864-- service retroactive to January 01, 2020
- HSA can pay for Over-the-Counter Medication: The CARES Act § 3702
- COVID-19 Testing & Treatment
 - Covered under plan
 - Meets HDHP minimum deductible
 - Notice 2020-15 – retroactive January 1, 2020

Cafeteria Plan Midyear Elections pg 301

Make	Make a new election on a prospective basis, if the employee initially declined to elect employer-sponsored health coverage;
Revoke	Revoke an existing election and make a new election to enroll in different health coverage sponsored by the same employer on a prospective basis; AND
Revoke	Revoke an existing election on a prospective basis, provided that the employee attests in writing that the employee is enrolled, or immediately will enroll in other health coverage not sponsored by the employer.
Make	Make new election, decrease or increase an existing election applicable to a health FSA on a prospective basis; OR
Revoke	Revoke an election, make a new election, decrease or increase an existing election applicable to dependent care assistance on prospective basis.

p. 301

Grace Period for Unused Amounts

Thru December 31, 2020

- FSA
- Dependent Care
- Carryover \$ 550

Polling Question 4

An HSA and an FSA are both use it or lose it plans.

True or False



Questions?