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26 CFR 601.105. Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.
(Also Part I, §§ 165; 1.165-1(c)(4), 1.165-1(d)(2)(iii), 1.165-7(a)(2), 1.165-7(b), 1.165-8(c).)

Rev. Proc. 2018-08

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SECTION 1. PURPOSE

.01 This revenue procedure provides safe harbor methods that individual taxpayers may use in determining the amount of their casualty and theft losses pursuant to § 165 of the Internal Revenue Code for their personal-use residential real property (as defined in section 3.02 of this revenue procedure) and personal belongings (as defined in section 3.03 of this revenue procedure). This revenue procedure provides additional safe harbor methods that may be used in the case of casualty and theft losses occurring as a result of any Federally declared disaster (as defined in section 2.06 of this revenue procedure).

.02 The Internal Revenue Service (IRS) will not challenge an individual's determination of the decrease in fair market value of personal-use residential real property if the individual qualifies for and uses one of the safe harbor methods described in section 4 of this revenue procedure. The IRS will not challenge an individual's determination of the decrease in fair market value of personal belongings if the individual qualifies for and uses one of the safe harbor methods described in section 5 of this revenue procedure.

.03 If an individual uses a safe harbor method described in this revenue procedure, the individual also must take into account the value of any no-cost repairs as described in section 6 of this revenue procedure.

.04 Use of a safe harbor method described in this revenue procedure is not mandatory. An individual may, instead, use the actual reduction in the fair market value of personal-use residential real property or personal belongings, pursuant to § 1.165-7(a)(2) of the Income Tax Regulations, if the individual has proper substantiation.

.05 The safe harbor methods provided in this revenue procedure apply only to the circumstances within the scope of this revenue procedure and may not be used in any other circumstances.

SECTION 2. BACKGROUND

.01 Section 165(a) generally provides that a taxpayer may deduct any loss sustained during the taxable year and not compensated for by insurance or otherwise. With respect to property not connected with a trade or business or a transaction entered into for profit, § 165(c)(3) limits an individual taxpayer's deduction to losses arising from fire, storm, shipwreck, or other casualty, or from theft.

.02 Section 165(h) imposes two limitations on casualty and theft loss deductions for property not connected with a trade or business or transaction entered into for profit. Section 165(h)(1) provides that any loss to an individual described in § 165(c)(3) shall be allowed only to the extent that the amount of the loss arising from each casualty, or from each theft, exceeds $100. Section 165(h)(2) provides that if personal casualty and theft losses for any taxable year exceed personal casualty and theft gains for the taxable year, the losses are allowed only to the extent of the sum of the amount of the gains, plus so much of the excess as exceeds ten percent of the adjusted gross income of the individual.

.03 Section 165(h)(4)(E) provides that to the extent an individual’s casualty or theft loss is covered by insurance, such loss shall be taken into account only if the individual files a timely insurance claim with respect to such loss.

.04 Section 165(i)(1) allows an individual who suffered a loss occurring in a disaster area and attributable to a Federally declared disaster to take the loss into account for the taxable year immediately preceding the taxable year in which the disaster occurred.

.05 Section 165(i)(4) authorizes the Treasury Department and the IRS to prescribe guidance under which an appraisal for the purpose of obtaining a loan of Federal funds or a loan guarantee from the Federal Government as a result of a Federally declared disaster may be used to establish the amount of any loss described in § 165(i)(1) or (2).

.06 Section 165(i)(5)(A) defines “Federally declared disaster” as any disaster subsequently determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act. Section 165(i)(5)(B) defines “disaster area” as the area so determined to warrant such assistance. For areas with respect to which Federally declared disasters have been determined, see www.fema.gov/disasters.

.07 Section 1.165-1(c)(4) provides that in determining the amount of loss sustained, adjustments must be made for any insurance or other compensation received.

.08 Section 1.165-1(d)(2)(iii) provides that if a taxpayer deducted a loss and in a subsequent taxable year receives reimbursement for such loss, the taxpayer does not recompute the tax for the taxable year in which the deduction was taken but includes the amount of such reimbursement in gross income for the taxable year in which received, subject to the provisions of section 111, relating to recovery of amounts previously deducted.

.09 Section 1.165-7(b) provides that the amount of a casualty loss is the lesser of (1) the difference between the fair market value of the property immediately before the casualty and the fair market value immediately after the casualty, or (2) the adjusted basis of the property. Section 1012 and § 1.1012-1(a) provide that the basis of property generally is its cost. Section 1016(a)(1) and § 1.1016-2(a) provide that the basis of property is adjusted for any expenditure, receipt, loss, or other item, properly chargeable to capital account, including the cost of improvements and betterments made to the property.

.10 Section 1.165-7(a)(2)(i) provides that to determine the amount of the deductible loss under section 165(a), the fair market value of the property immediately before and immediately after the casualty generally shall be ascertained by competent appraisal. Section 1.165-7(a)(2)(ii) provides that the cost of repairs to the property damaged is acceptable as evidence of the decrease in value of the property if the taxpayer shows that: (1) the repairs are necessary to restore the property to its condition immediately before the casualty; (2) the amount spent for such repairs is not excessive; (3) the repairs do not care for more than the damage suffered; and (4) the value of the property after the repairs does not, as a result of the repairs, exceed the value of the property immediately before the casualty. In order to use the cost-of-repairs method to determine the decrease in fair market value, the taxpayer must actually make the repairs rather than rely on estimates of repairs that will be performed in the future or not at all. See Lamphere v. Commissioner, 70 T.C. 391, 396 (1978), acq., 1978-2 C.B. 2; Farber v. Commissioner, 57 T.C. 714, 719 (1972), acq., 1972-2 C.B. 2.

.11 Section 1.165-8(c) provides that the amount deductible in the case of a theft loss is determined consistently with the manner described in § 1.165-7 for determining the amount of a casualty loss. The fair market value of the property immediately after the theft is considered to be zero.

.12 Section 1.165-7(b)(2)(ii) provides that in determining a casualty loss involving real property and improvements thereon not used in a trade or business or in any transaction entered into for profit, the improvements (such as buildings and ornamental trees and shrubbery) to the property damaged or destroyed are considered an integral part of the property, and no separate basis need be apportioned to the improvements.

.13 Following certain disasters, Congress may modify the rules of § 165 as applied to casualty and theft losses occurring in a specified disaster area. For example, § 504(b) of the Disaster Tax Relief and Airport and Airway Extension Act of 2017, Pub. L. No. 115-63, 131 Stat. 1168, 1182-1183 (Sept. 29, 2017), modifies the § 165(h) loss limitations and other provisions of § 165 as applied to casualty and theft losses occurring in certain areas affected by Hurricanes Harvey, Irma, and Maria.

.14 Taxpayers report gains and losses from casualties and theft on Form 4684 according to the Form 4684 instructions, as updated at www.irs.gov/form4684. See special instructions at www.irs.gov/form4684 for taxpayers electing under § 165(i) to report their casualty and theft losses calculated under this revenue procedure on an original or amended 2016 tax return.

.15 The Treasury Department and the IRS are aware that taxpayers often have difficulty determining the amount of their losses under the methods provided in § 1.165-7(a)(2), which has resulted in time-consuming and expensive litigation. In order to provide certainty to both taxpayers and the IRS, this revenue procedure provides safe harbor methods that individuals may use under § 1.165-7(a)(2) to measure the decrease in the fair market value of their personal-use residential real property following a casualty and to determine the pre-casualty or theft fair market value of personal belongings.

The Treasury Department and the IRS also are aware of the unique circumstances surrounding a Federally declared disaster area and the difficulties individuals encounter in determining the amount of their losses in those areas. Accordingly, this revenue procedure provides those individuals with additional safe harbor methods to use in determining the amount of their casualty and theft losses for property damaged, destroyed, or stolen as a result of any Federally declared disaster.

SECTION 3. SCOPE

.01 In general. An individual who suffered a casualty loss to the individual's personal-use residential real property may use the safe harbor methods provided in sections 4.02, 4.03, or 4.04 of this revenue procedure in determining the amount of the individual's casualty loss under § 165. An individual who suffered a casualty loss to the individual's personal-use residential real property due to a Federally declared disaster may use any of the safe harbor methods provided in section 4 of this revenue procedure in determining the amount of the individual's casualty loss under § 165. An individual who suffered a casualty or theft loss to the individual's personal belongings may use the safe harbor method provided in section 5.01 of this revenue procedure in determining the amount of the individual's casualty and theft loss under § 165. An individual who suffered a casualty or theft loss to the individual's personal belongings due to a Federally declared disaster may use either of the safe harbor methods provided in section 5 of this revenue procedure in determining the amount of the individual's casualty and theft loss under § 165.

.02 Definition of personal-use residential real property and personal residence. For purposes of this revenue procedure, personal-use residential real property is real property, including improvements (such as buildings and ornamental trees and shrubbery), that is owned by the individual who suffered a casualty loss and that contains at least one personal residence. Personal-use residential real property does not include a personal residence if any part of the personal residence is used as rental property or contains a home office used in a trade or business or transaction entered into for profit. For purposes of this revenue procedure, a personal residence is a single family residence, or a single unit within a contiguous group of attached residential units (for example, a townhouse or duplex), owned by the individual who suffered a casualty loss, and includes any structures attached to the residence or single unit. For purposes of this revenue procedure, a personal residence does not include a condominium or cooperative unit, or any other property for which the individual who suffered the casualty loss does not own the structural components of the building (such as the foundation, walls, and roof), or owns only a fractional interest in all of the structural components of the building, or a mobile home or trailer.

.03 Definition of personal belongings. For purposes of this revenue procedure, a personal belonging is an item of tangible personal property that is owned by the individual who suffered a casualty or theft loss and that is not used in a trade or business or in a transaction entered into for profit. For purposes of this revenue procedure, personal belongings do not include a boat, aircraft, mobile home, trailer, or vehicle (as defined in section 5.02(2) of this revenue procedure), or an antique or other asset that maintains or increases its value over time.

.04 Taking into account no-cost repairs. An individual using a safe harbor method described in this revenue procedure must take into account the value of any no-cost repairs as described in section 6 of this revenue procedure.

.05 Limited use of safe harbor methods. The safe harbor methods described in sections 4 and 5 are available only in the circumstances described in this revenue procedure.

SECTION 4. PERSONAL-USE RESIDENTIAL REAL PROPERTY SAFE HARBOR METHODS

.01 In general. An individual within the scope of this revenue procedure may use one of the safe harbor methods described in this section 4. If an individual owns two or more parcels of personal-use residential real property, the use of a safe harbor method for one parcel does not require the individual to use the same safe harbor method, or any safe harbor method, for any other parcel.

.02 Estimated Repair Cost Safe Harbor Method. Under the Estimated Repair Cost Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may use the lesser of two repair estimates prepared by two separate and independent contractors, licensed or registered in accordance with State or local regulations. The two repair estimates must set forth the itemized costs to restore the individual's personal-use residential real property to the condition existing immediately prior to the casualty. However, the costs of any improvements or additions that increase the value of the personal-use residential real property above its pre-casualty value, such as the cost to elevate the personal residence to meet new construction requirements, must be excluded from the estimate for purposes of this safe harbor. The Estimated Repair Cost Safe Harbor Method is available for casualty losses of $20,000 or less, prior to application of the limitations under § 165(h).

.03 De Minimis Safe Harbor Method. Under the De Minimis Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may estimate the cost of repairs required to restore the individual's personal-use residential real property to the condition existing immediately prior to the casualty. However, the costs of any improvements or additions that increase the value of the personal-use residential real property above its pre-casualty value, such as the cost to elevate the personal residence to meet new construction requirements, must be excluded from the estimate for purposes of this safe harbor. An individual's estimate must be a good-faith estimate, and the individual must maintain records detailing the methodology used for estimating the loss. The De Minimis Safe Harbor Method is available for casualty losses of $5,000 or less, prior to application of the limitations under § 165(h).

.04 Insurance Safe Harbor Method. Under the Insurance Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may use the estimated loss determined in reports prepared by the individual's homeowners' or flood insurance company setting forth the estimated loss the individual sustained as a result of the damage to or destruction of the individual's personal-use residential real property.

.05 Safe harbor methods for Federally declared disasters. An individual who suffered a casualty loss to personal-use residential real property in a disaster area and due to a Federally declared disaster may use one of the following safe harbor methods in determining the amount of the individual's casualty loss under § 165.

(1) Contractor Safe Harbor Method. Under the Contractor Safe Harbor Method, to determine the decrease in the fair market value of the individual's personal-use residential real property, an individual may use the contract price for the repairs specified in a contract prepared by an independent contractor, licensed or registered in accordance with State or local regulations, setting forth the itemized costs to restore the individual's personal-use residential real property to the condition existing immediately prior to the Federally declared disaster. However, the costs of any improvements or additions that increase the value of the personal-use residential real property above its pre-disaster value, such as the cost to elevate the personal residence to meet new

construction requirements, must be excluded from the contract price for purposes of this safe harbor. To use the Contractor Safe Harbor Method, the contract must be a binding contract signed by the individual and the contractor.

(2) Disaster Loan Appraisal Safe Harbor Method. Under the Disaster Loan Appraisal Safe Harbor Method, to determine the decrease in fair market value of the individual's personal-use residential real property, an individual may use an appraisal prepared for the purpose of obtaining a loan of Federal funds or a loan guarantee from the Federal Government setting forth the estimated loss the individual sustained as a result of the damage to or destruction of the individual's personal-use residential real property from a Federally declared disaster.

SECTION 5. PERSONAL BELONGINGS SAFE HARBOR METHODS

.01 De Minimis Safe Harbor Method. Under the De Minimis Safe Harbor Method, an individual may make a good faith estimate of the decrease in the fair market value of the individual's personal belongings. An individual using the De Minimis Safe Harbor Method must maintain records describing the personal belongings affected and detailing the methodology used for estimating the loss. The De Minimis Safe Harbor Method is available for casualty or theft losses of $5,000 or less, prior to application of the limitations under § 165(h).

.02 Safe harbor method for Federally declared disasters.

(1) Replacement Cost Safe Harbor Method. Except as provided in section 5.02(2) of this revenue procedure, an individual may use the safe harbor method in this section 5.02(1) to determine the fair market value of the individual's personal belongings located in a disaster area immediately before a Federally declared disaster in order to

compute the amount of a casualty or theft loss. If an individual chooses to use the Replacement Cost Safe Harbor Method for a Federally declared disaster, the individual must apply that method to all personal belongings for which a loss is claimed under § 165 for that Federally declared disaster, except those specifically excluded in section 5.02(2) of this revenue procedure.

To use this safe harbor method, an individual must first determine the current cost to replace the personal belonging with a new one and reduce that amount by 10% for each year the individual owned the personal belonging using the percentages in the Personal Belongings Valuation Table below. If the personal belonging was owned by the individual for nine or more years, the pre-disaster fair market value is 10% of the current replacement cost under this safe harbor method.

Personal Belongings Valuation Table	
Year	Percentage of Replacement Cost to Use
1	90%
2	80%
3	70%
4	60%
5	50%
6	40%
7	30%
8	20%
9+	10%

To determine the amount of a casualty or theft loss for personal belongings that were damaged, destroyed, or stolen:

(a) Determine the decrease in the fair market value of each personal belonging by subtracting the fair market value of the personal belonging immediately after the Federally declared disaster from the fair market value of the personal belonging immediately before the Federally declared disaster, determined as described above. If a personal belonging was destroyed or stolen as a result of a Federally declared disaster, its fair market value after the disaster is zero.

(b) Determine the basis of each personal belonging (generally its cost).

(c) Compare the decrease in fair market value (from step (a)) with the basis of the personal belonging (from step (b)). From the lesser of the basis or decrease in fair market value, subtract any insurance or other reimbursements the individual receives or expects to receive for the personal belonging.

(2) Exclusions. An individual may not use the Replacement Cost Safe Harbor Method for Federally declared disasters for a boat, aircraft, mobile home, trailer, vehicle, or an antique or other asset that maintains or increases its value over time. For purposes of this revenue procedure, a vehicle is an automobile, motorcycle, motor home, recreational vehicle, sport utility vehicle, off-road vehicle, van, or truck.

An individual may determine the pre-disaster value of a boat, aircraft, mobile home, trailer, or vehicle by consulting established pricing sources. See Rev. Rul. 2002-67, 2002-2 C.B. 873; Publication 561, Determining the Value of Donated Property.

(3) Example. An individual's personal belongings included a couch destroyed by a hurricane in a Federally declared disaster area. The individual purchased the couch for $700 four years prior to the hurricane. The cost to replace the couch with a new couch is $1,000. The couch is not insured.

Using the Replacement Cost Safe Harbor Method for Federally declared disaster areas, the individual computes the fair market value of the couch immediately before the hurricane by multiplying the current replacement cost of the couch, $1,000, by the applicable percentage of replacement cost from the Personal Belongings Valuation table, 60%:

$$\$1,000 \times 60\% = \$600$$

The individual determines the decrease in the fair market value of the couch by subtracting $0, the fair market value of the couch immediately after the hurricane, from $600, the fair market value of the couch immediately before the hurricane.

$$\$600 - 0 = \$600$$

The individual compares the basis of $700 with the decrease in fair market value of $600. Since the decrease in fair market value is less than the basis, the amount of the individual's casualty loss is $600.

SECTION 6. REDUCTION FOR NO-COST REPAIRS

Under § 165(a), a casualty loss must be reduced by insurance or other amounts received, such as amounts given to an individual to repair the damage to the individual's property due to the casualty. This includes the value of repairs to, or rebuilding of, the individual's personal-use residential real property provided by another party at no cost to the individual ("no-cost repairs"), such as the repair or rebuilding of an individual's personal residence by volunteers. No-cost repairs include repairs made for a de minimis or token cost, donation, or gratuity.

An individual who uses any safe harbor method provided in this revenue procedure to determine the decrease in the fair market value of or the amount of loss to the individual's personal-use residential real property or personal belongings must reduce the loss by the value of any no-cost repairs.

SECTION 7. EFFECTIVE DATE

This revenue procedure is effective December 13, 2017**.**

SECTION 8. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-0074. Please refer to the Paperwork Reduction Act statement accompanying Form 1040, U.S. Individual Income Tax Return, for further information.

SECTION 9. DRAFTING INFORMATION

The principal author of this revenue procedure is Joanna L. Trebat of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue procedure, contact Ms. Trebat at 202-317-7003 (not a toll-free call).