



Casualty Loss and Compliance

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Casualty loss in a Low-Income Housing Tax Credit (LIHTC) project can create serious compliance issues and financial concerns for an owner/investor.

Casualty loss is defined by the IRS as “damage, destruction, or loss of property resulting from an identifiable event that is sudden, unexpected, or unusual” ([IRS 8823 Audit Technique Guide](#), Chapter VI, Section C.5).

Examples of casualty loss are fires, floods, storms, earthquakes, tornados, vandalism, and even methamphetamine contamination.

“Physical damage to LIHTC projects caused by casualty events and which render LIHTC residential rental units or buildings, or common areas associated with the property, unsuitable for occupancy is reported as noncompliance with the UPCS or local standards” and typically means a reduction in the qualified basis ([IRS 8823 Audit Technique Guide](#), Chapter VI, Section C.5). Casualty loss can result in the loss of current year credits and/or the recapture of accelerated credits already claimed. Current credits and previously claimed credits are treated differently.

For casualty loss that is **not** subject to a Presidentially declared major disaster, an owner cannot claim new credits while the unit(s) is uninhabitable unless it is made suitable for occupancy by year end. If the unit(s) is not restored by year end, it will not generate any credits for the entire year. As for previously claimed credits, per Section 42 of the Internal Revenue Code, if the area is restored within a reasonable period of time, there will be no recapture of such credits ([26 U.S.C. § 42\(j\)\(4\)\(E\)](#)).

The state agency must report the loss on IRS Form 8823 and indicate the loss was beyond the owner’s control. The state agency will give a correction period before filing the IRS form 8823. The timeline will vary depending on the severity of the loss. For casualty loss, the timeline can be up to 24 months from the end of the calendar year when the loss took place under IRS rules. If all deficiencies are resolved within the correction period, the IRS form 8823 will be filed as corrected.

We hope your project never experiences a casualty loss event, especially late in the year as units may not be repaired/restored by year end.

What happens when it does and what steps do you take to report and fix the noncompliance?



1. The owner must promptly report the loss to the state agency and provide the following:
 - The date of loss
 - The unit, building number, and/or location of all out of service areas
 - A written statement describing the cause of the loss and nature of damage
 - An estimated date the repair or reconstruction will begin and estimated date for completion

Check with your state agency on any additional reporting requirements.

2. Owners must prioritize repairs to meet deadlines to restore any damaged unit/building and place them back online before December 31 to avoid a loss of credit for the year.
3. Once the unit/building is restored, notify the state agency repairs are complete and the units are habitable. Provide the following documentation to the state agency:
 - A written summary of repairs made
 - The date each unit or area was brought back online
 - Copies of invoices, work orders, etc.
 - Photos

By maintaining strong communication with your state agency, and by adhering closely to IRS guidance, owners and management agents can safeguard their development and limit the loss or recapture of credits. Remember, it is critical to consult your tax accountant as well.

Resources on casualty loss:

- [\(26 U.S.C. § 42\(i\)\(4\)\(E\)\).](#)
- [IRS 8823 Audit Technique Guide](#), Section C.5
- Various Revenue Procedures and IRS guidance

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